Issues and Alternatives – 1977

The Process of Public Decision-Making

Ontario Economic Council

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Preface

A year ago, the Ontario Economic Council issued a series of papers on "Issues and Alternatives" in six areas of major concern for public policy in Ontario and in Canada. These papers focussed on public expenditure policies in the fields of health, housing, education and social security, as well as on policies related to national independence and the development of northern Ontario.

As a direct extension of its work in these areas, the Council is now issuing three additional papers under the general heading of "Issues and Alternatives". These concentrate on the outlook for the Ontario economy during the next decade, the public decision-making process and intergovernmental relations. The purpose of these papers, as of those published earlier, is to highlight major issues, as we see them, to stimulate informed public debate on these issues and to provide a framework for discussion about possible improvements in government policies.

In the Council's view, this paper attempts to elucidate the complex process whereby governments arrive at decisions in such areas as health, housing, education and social security policy. In effect, it challenges the common notion of "the public interest" as a central principle of policy making. Instead, it emphasizes that, just as in the private sector, self-interest and the incentives for those participating in the process play a major role in determining what decisions are made (and not made). This way of looking at the process, in our view, gives a different perspective both on the role of government in our society and on the appropriate design of policies. The paper also offers a number of suggestions about how the decision process might be improved.

Although this subject differs notably from those usually considered in discussions of public policy, we believe it is a basic issue that deserves much deeper understanding and examination than it has had in the past, given the present size and complexity of government. It is the Council's hope that this report will focus attention on this issue and thereby contribute to the improvement of policies at all levels of government.

While each member of the Ontario Economic Council does not necessarily subscribe to everything contained in this report, the report does reflect a consensus of the members.

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Summary and Main Policy Issues

When the objectives of government are stated in sufficiently general terms, there seems to be much agreement among people. Governments should ensure full employment, stable prices and economic growth. Governments should enhance economic efficiency. Governments should ensure a more equitable distribution of income. Governments should maintain our individual freedoms. The pursuit of these objectives is often described as being "in the public interest". The implication is, of course, that they could not be realized solely by the private sector acting on its own. Seen in these terms the adoption of the collective objectives just cited would seem to permit differentiation of the respective roles of the public and private sectors and a choice among alternative government policies. But, as we all know, the issues are not that simple. There is, and probably always will be, conflict among individuals and interest groups.

There are several reasons for this conflict. One of the reasons is that many of the objectives are themselves in conflict. For example, more economic growth might perhaps produce greater income inequality. Full employment may mean more inflation, and so on. When such conflicts arise, how much weight should be given one objective relative to others? And who decides what the relative weights should be when, as is invariably the case, the electorate is not unanimous?

Even at a technical level, there is often conflict about what the trade-offs are among competing objectives as distinct from what price should be paid for the greater realization of one objective in terms of another that may have

been foregone. Perceptions differ about *actual* trade-offs and they certainly differ about who should gain and who should lose when hard choices have to be made. Resolving, if not solving, these endless conflicts is at the heart of the political process. Different political processes almost certainly bring about different resolutions of these conflicts which ostensibly concern abstract government policies but are often simply the conflicts among individuals with different interests.

An Approach to Analysing Decision-Making

The Ontario Economic Council is of the opinion that an understanding of our government decision-making process and of how it reconciles the conflicting interests of individuals and groups is vital to an understanding of the role of government, its expansion and growing complexity, and the improvement of policies.

Some insights developed by economists to analyse the decision-making process in the private sector have recently been adapted to the analysis of collective decision-making. This paper in part seeks to make this analytic framework available to a wider audience and to illustrate its potential usefulness by applying it to some aspects of a few major issues that the Council has commented upon in the recent past. The paper is not set forth as a substitute for more traditional forms of analysis but rather as a complement to them.

The basic idea set forth in this paper is straightforward. It is assumed that there are three systems relevant to our purpose: the political system, the bureaucratic system, and the special interest group system. Each of these systems consists of a number of organizations that themselves consist of groups or individuals.

Each of these systems has quite distinct sets of rules, some formal and some informal. These rules determine the incentives and disincentives under which the individuals actively engaged in a particular system operate. In short, they induce certain kinds of behaviour as individuals seek to maximize their rewards; and they inhibit other kinds of behaviour as individuals seek to minimize their penalties. Examples are legion and diverse: a subsidy rule (law) may induce more production; a zoning rule (bylaw) may inhibit the construction of high density housing.

Individuals, trying to maximize their personal satisfactions, in general, behave in accordance with these pay-off rules. Change the pay-off rules and individual and organizational behaviour is changed – for better or for worse depending on the outcome desired. The incentives and disincentives of different organizations and the institutional arrangements among organizations seem to explain much of the behaviour of the members of the several groups involved in the political process.

It is important to recognize, too, that because the incentive rules differ among each of the several systems the kinds of players selected and their behaviour in each system differ.

Two additional points need to be made. Usually there are what are called "meta" rules – rules about how the rules in a particular system can be altered: a formal or informal constitution. The political constitution usually spells out to some degree, among other things, the rules that determine the relationships among the various systems. Changes in these meta rules obviously have the greatest leverage in the sense that a change in a meta rule may bring about changes in thousands of other lesser rules.

Some Implications of the Approach

Let us consider some examples of the implications of this analysis of collective decision-making:

(a) In two-party states, where a majority vote is needed for election, the analysis suggests that the two parties will tend to have similar platforms which conform to the preferences of the middle-of-the-road voter.

(b) Voters consider the potential costs and benefits to themselves, both direct and indirect, of various political platforms and cast their ballots to support the platform offering the greatest net benefits.

(c) Large groups of individuals sharing a common interest often have difficulty in forming a cohesive lobby group, even when there are net benefits to each member, because individuals have an incentive not to join if the group would continue to exist without them. This "free rider" problem means that small groups are likely to organize more effectively than large groups, in the absence of rules which secure compulsory membership.

(d) As a final example, the analysis suggests incentives for government officials to increase efficiency in their departments may not be strong because rewards cannot easily be tied to performance.

To look at collective decision-making in this way is not to deny that many individuals are often motivated by compassion. Rather it is to argue that more insights into collective decision-making are gained if we understand the effects on the behaviour of individuals of the rules (incentives) of large organizations and of the institutional framework within which they operate.

Some General Conclusions

In examining the process of collective decision-making the Council has reached a number of general conclusions:

(a) The transactions costs (information and negotiating costs) in terms of the time, effort and resources used in this method of reaching decisions appear to be high and rising. While accepting the inevitability of conflict among groups, as seen from this "self-interest" perspective, it seems to be true that our costs would be reduced with a relatively smaller government sector and a more competitive private sector. Why have these transactions costs become so enlarged? Two points seem especially germane. Firstly, in the face of price inflation and rapid technological and social change individuals have become more uncertain about their future both in terms of relative and absolute well-being. As a consequence they have organized into groups and sought to reduce their uncertainty by demanding more government action. Secondly, other individuals and groups, perceiving their relative positions to have been eroded by government actions, have sought to have government restore their positions.

(b) The decision process seems to produce certain outcomes which are inefficient. Through redesign, many programs could make the intended beneficiaries just as well off and use fewer resources or impose fewer external costs. However, there are usually some groups that lose from any given policy change. They are often well organized, and strongly resist policy changes which would affect them adversely.

(c) The system seems to have made so many changes in policy recently that the level of uncertainty has increased in our society. In our mixed economy, in which many of our common goals are achieved by setting up rules and incentives that influence the decisions of the private sector, frequent rule changes can have perverse effects. Ever-changing policies appear to be more debilitating than helpful in our present environment.

Basic Recommendations

The Council is of the opinion that a number of basic reforms would contribute to improvement in the performance of our collective decision process:

(a) More openness and disclosure of government activities would reduce the ability of special interest groups to secure benefits to

themselves and provide an incentive to politicians and civil servants to achieve greater efficiency in the provision of services. Possible changes might include strengthening the Committees of the Legislature, more detailed reporting of regulatory activities, fuller reporting of the costs and benefits to taxpayers of tax concessions and disclosure of the background data used in reaching a government decision.

(b) Improvement in efficiency might be realized by increasing the information on departmental performance available to the public and to the legislature.

(c) The government-engendered conditions which sustain the power of special interest groups should be examined and perhaps some of them eliminated. The self-regulatory powers of professional groups might be constrained although presumably they cannot be eliminated.

Although these recommendations are familiar, they are, in the Council's opinion, the kind of basic reform required. Sometimes the obvious needs to be reemphasized.

Applying the Approach: Four Examples

To further explore the "self-interest" approach to analysing government decision-making, four policy issues were examined. One example was taken from each of four policy areas on which the Ontario Economic Council has been focusing its activities: social security, housing, health and education. Last year the Council published policy papers in these areas which highlighted the principal issues and offered a framework for discussion about improvements in government policies.

MINIMUM WAGE LAWS

The use of the minimum wage laws offers both direct and indirect costs and benefits to several groups. Workers who remain employed at the minimum wage and organized labour seem to be beneficiaries. Workers who lose their jobs because of reduced demand for labour and owners of businesses employing low-wage labour seem to be the main losers. Minimum wage laws are attractive to a politician because they incur only a small budget cost and appear to assist the working poor. The use of this method of assisting the working poor, as opposed to a cash income supplement or a training program, seems better explained by the interaction of voters, interest groups and politicians in the political process rather than by a claim that the law is a "good" or "efficient" policy. The geographic dispersal of the workers who

lose their jobs and the "free rider" problem seem to explain why those who are hurt by this legislation are not a more vocal opposition.

SUBDIVISION APPROVAL

The process of approving new developments in Ontario seems to encourage subdivisions with large lots and, by implication, large expensive houses. This seems explainable by the influence local councils have over the nature of subdivisions through bylaws and subdivision agreements. Local councils, interested in seeking re-election, seek those developments which produce the maximum net benefits for their voters, in particular those developments which do not raise the taxes of existing residents. The interests of potential consumers of smaller lots and houses are not well-represented in the decision process.

HOSPITAL REIMBURSEMENT

In Ontario, a number of budgetary changes have been introduced designed to contain or even reduce hospital expenditures through improvements in efficiency and reduced hospital usage. The approach of analysing the separate participants as pursuing their self-interests within the incentive structure of the hospital system suggests little constraint on the growth of expenditures could be expected. This indeed was the case. The incentives of the reforms encouraged the hospital trustee board and administrator to hold expenditures but did little to encourage efficiency. The reforms offered no incentives for the physician to change his crucial decisions regarding hospital utilization and length of stay.

FINANCING HIGHER EDUCATION

The Ontario Council on University Affairs (OCUA) was established to act as an independent buffer group between educational institutions who want more money and autonomy and the government which seeks to spend less money and permit intellectual freedom. OCUA probably has succeeded in obtaining more money for post-secondary education than would otherwise be the case and, in return, has accepted the onerous responsibility of recommending how available funds should be divided among universities. In a sense OCUA is a double-edged sword from the government's point of view: it is another painful pressure group but it reduces the political embarrassment of choosing among institutions and defuses the charge of direct government interference with academic freedom that otherwise would arise. At the present time universities and colleges are not, in effect, allowed to alter their fees except by stated amounts. If, for example, the government eliminated this rule the allocation of resources among them presumably would be quite different than that which exists under OCUA and might reduce the need for a buffer organization.

1
Introduction

There has been extensive study of some aspects of the growth of the modern state with its rapidly expanding income transfer programs, massive resource commitments to health and education, and with its programs to regulate many sectors of the economy and of society. Research has been addressed primarily to three questions.

First: what criteria should be used to assess the efficiency, effectiveness and equity of actual or proposed programs?

Second: what are the effects of government intervention? Unless the direct and indirect impact of expenditures, taxes and regulations are known it is impossible to judge the merits of existing programs and policies or the merits of potential changes in them.

Third: what factors influence the demand for changes in government policies and programs? Changes in tastes? Changes in population? Changes in income? Changes in decision-making processes? Changes in other factors?

The Ontario Economic Council has sponsored research by qualified persons in a broad range of policy areas and, as a stimulus to public debate, released papers which have dealt with some of the principal issues. The Council has suggested alternative policy approaches which it felt warranted further examination. Last year the Council published papers dealing with health, housing, education, social security, national independence and northern development.

However, most of the Council's work heretofore has focused on the first two questions. Curiously, economists have addressed the last of the three questions – the determinants of the nature and extent of government activity – with much less vigour than the first two. This is probably explained in part by their belief that the answers to the third question could not be provided by the tools available to them. In part also it may reflect an inclination to develop economics as a value-free science, yielding testable hypotheses. And in part it may be accounted for by a naive presumption that bad policies (as seen by the individual economist) are simply the result of ignorance. Having specified what constituted a "good" policy (again in their own eyes) many economists apparently feel that they have satisfied their obligation.

Most of the work which has been done on the determinants of government activity has not directly considered the nature of the government decision-making process. Rather it has identified such things as rising incomes, increasingly complex spillover effects, urbanization, changing tastes, the increasing revenues generated by an unchanged tax system, or productivity differentials between the public and private sectors. Rarely have the links between the determinants (for example rising incomes) and the results (for example increased expenditure for public parks) been addressed explicitly. It is on this link, the government decision-making process, that this paper focuses.

In Chapter One there is a discussion of the difficulty of establishing criteria to determine appropriate government activities. There seems to exist a broad consensus about what government ought to do, although only if defined in extremely general terms. This consensus disintegrates when specific rules are offered or when specific policies are to be assessed. In this situation, the process we have in society for collectively deciding on government actions – the political process – is of critical importance.

In Chapter Two, a method of analysing the political decision-making process is presented. At the centre of this analysis is the assumption that politicians, voters, and civil servants are really no different than businessmen, professionals and workers – all make their decisions in terms of maximizing their net benefits, broadly conceived. No doubt individuals make some decisions that benefit others at personal cost. Some politicians are interested not simply in election or re-election but in implementing their vision of a fair society. Some civil servants are interested only in offering advice to improve public policy formation – just as some businessmen and workers are not only interested in profits and wages but also in helping the disadvantaged. But for *analytical* purposes the hypothesis that seems to explain collective decision-making best is that individuals seek their self-interest under the rules that constitute the particular incentive system within which they operate. This is not to say that most individuals are amoral, much less immoral. Rather it is to recognize that most of the time most people make their decisions consis-

tent with the pursuit of rewards and the avoidance of punishments.

Politicians, government officials, journalists, businessmen, interest group leaders, members of professional associations and other groups are not minor Satans or junior Machiavellis. The point is that individuals in different groups make their decisions under quite different and distinct sets of rules. The result is that they decide differently in response to the differences among their respective incentive systems. These different incentive systems, the rules that determine how these incentives are changed, and the rules that determine how the groups relate to each other, seem to explain many of the changes in public policies.

In Chapter Three an application is presented of this framework to four public policy problems in the areas of health, housing, education and social security. The objective in this Chapter and throughout the paper is not to provide a critique of current programs or a blueprint for reform. Rather it is to provide a better understanding of the government process. It is hoped that with such an understanding an improved perspective on our current problems will be reached and a sounder basis for achieving future reforms can be developed.

2
Deciding the Role of Government

There seems to exist a consensus in Canada and in Ontario about the appropriate role for government, but only if this role is stated in extremely general terms. Most generally, government should act in the public interest. More specifically, government should ensure full employment, economic growth and stable prices; it should act to increase productivity and economic efficiency; it should act to preserve individual freedom and to secure greater equality of opportunity; it should ensure a just distribution of income, an improved environment, regional development, an enhanced lifestyle and greater political, cultural and economic independence.

Naively, one might believe that such a consensus would permit the development of rules or criteria to select the appropriate activities of governments. These rules would be used to decide among alternative government policies and to decide which activities should be in the public sector and which in the private.

However, when specific programs or proposals are considered, the hope that rules could be formulated is largely unrealized. The "public interest" proves to be a very illusive concept. The consensus about broad goals is not sustained in the assessment of current actions or the consideration of new programs.

This inability to sustain a consensus or to develop rules seems to be the product of a number of factors. There is disagreement about the impact of government activities on the generally accepted goals. Does a given program enhance the Canadian lifestyle? Does our fiscal and monetary policy encourage economic growth and stable prices? Does our tax treatment of the costs of advertising in foreign-owned publications increase our cultural independence?

Another source of disagreement arises when one attempts to make the general goal more specific. Is joint planning of resource exploitation a loss of our national independence or simply international cooperation? What is a desirable Canadian lifestyle? What is a just distribution of income?

Probably the most fundamental source of disagreement arises because of the inevitable trade-offs among the goals. To come closer to one goal almost inevitably involves moving away from another. If the achievement of one goal demands resources, time or effort, these cannot be used in pursuit of another. To have a more just distribution of income may mean reduced economic growth. To improve the environment may mean undesired restrictions on how we spend our leisure time. To reduce inflation may reduce economic growth, at least in the short run. We cannot seem to agree about the optimum configuration of goals. Examples of each of these sorts of disagreement are discussed at greater length below.

It is interesting to note that some of the difficulty in discussing the appropriate role of government stems from the problems of defining and measuring the government sector. This difficulty has been especially evident in recent debates over whether we have too much government. It is probably useful at the outset in this discussion of the role of government to sketch first the broad dimensions of the government sector in Canada.

Measuring the Size of Government

It is paradoxical that an issue debated with such spirit as the role of government should so frequently revolve about an elusive measurement: the size of the government.[1] The boundaries of the government sector are not easily established. They are set at one point for certain purposes and elsewhere for others. Should crown corporations (such as Air Canada), which derive most of their revenue from the sale of services, be considered part of government? Should consulting or construction firms doing business almost exclusively with governments or educational institutions be included as part of the public sector? How should borrowing from the pension plans of government employees be treated?

Certain activities, although obviously part of government, have not and probably cannot be measured. How does one measure, for example, the regulatory activity of agencies such as the Ontario Municipal Board, or the Canadian Radio-Television and Telecommunications Commission? How does one measure the advertising campaigns designed to change lifestyles, to encourage health-promoting exercise or reduce the consumption of cigarettes or alcohol? Certainly data on government expenditure and on the number of government employees are inadequate measures.

Moreover, other public sector policies, while measurable in principle, are

never recorded. Most notable are tax concessions. Suppose government decided to exempt income earned from the practice of law. In the short run this decision would transfer money to lawyers just as surely as industrial incentive grants now transfer money to firms. Yet the latter would appear in the public accounts as an expenditure. The former would not. Alternatively, suppose family allowance payments to tax-paying families were stopped and replaced by an additional dependent child exemption. Suppose the exemption were designed so that all families with children had the same after-tax income as they have with it: they would be just as well off. Expenditure and revenue data would show a decline in the size of government. But would the size of government have been changed in any real sense?

Much of the debate concerning the size of the government sector concentrates on explicit expenditures, tax collections and borrowing. This is because these activities comprise most of what is *normally* considered government activity and because they are easily documented. The data are frequently expressed in relative terms: government cash inflows or outflows are given as a fraction of the money value of the output of the national or provincial economy. (Absolute measures ignore the growth of population and of income). The most commonly cited measure of the relative size of government in our society is the ratio of total government expenditure to gross national product at market prices. The ratio of expenditure by all levels of government to gross national product stood at 0.41 in 1975 (Table 1, Appendix). This ratio has been rising during the 1970s. During the early 1950s the ratio remained relatively constant at about 0.27.

Considerable care must be exercised, however, in interpreting the ratio. Its use by many commentators reflects a basic misunderstanding of what it measures. It does *not* mean that 42 percent of our output was produced by the public sector. Gross national product is a measure of the value of the final output produced during one year. It sums the value of all the private output (the money value of cars, housing, accounting services, movies produced) and the money value of all public services (the money value of health services, education, and police protection produced). Government expenditures on these kinds of items are taken to be their money value and are used in the summation to compute the gross national product.

But not all government expenditures are used to produce public services. Much of what is recorded as government spending is, in fact, transfer payments. Money is transferred from one group to another: from the employed to the unemployed via unemployment insurance; from childless taxpayers to families via family allowances; from wealthier taxpayers to poorer individuals via welfare payments. An increase in transfer payments changes the pattern of who has the money to spend in our society. It does not increase the fraction of our output produced by government. Transfer payments do not constitute a collective decision about what goods are to be produced, as

in the case of highways for example. Rather they constitute a collective decision about how income is to be distributed in the private sector. The recipients of transfers use the income just as they would privately earned income, to pay taxes and to purchase goods in the private decentralized market.

Better measures of the relative role of government in society are available if one divides government expenditures into two parts: expenditures which result in the production of public goods and services and those that are essentially transfer payments.

Government expenditures that result in the production of public goods and services, expressed as a ratio to the total output of our economy, provides an approximate measure of how much of total output is produced by the public sector (recognizing of course that the value of public services had to be measured as the cost to produce them).

By this measure about 24 percent of our output is produced by government. This has been constant over the 1970s, having risen from about 18 percent in the early 1950s (Table 1, Appendix). This indicator shows a smaller role for government in our society and a much less rapid increase in its size in the post-war period. Remarkably, when this measure is adjusted for price changes, the share of total output produced by government has remained unchanged since about 1950 (Table 1, Appendix). The rapid increase in government spending does *not* mean we have relatively more public services and fewer private. This constancy is all the more remarkable when one considers the rapid growth of public expenditures on health and education. In conjunction with the rapid increase in the production of these public services there has been a relative decline in the production of others, in particular national defence.

Rough confirmation for these conclusions is offered by one body of data on employment in the public sector. A comprehensive calculation of government employment in even one year is very difficult and almost impossible to develop over several years. Many agencies which are part of government do not report employment figures to any central authority. One consistent series exists on general government employees at the federal, provincial and local levels. These data record what most people consider as civil servants; for example, in the education field they count workers at the Ministry of Education but not teachers or school maintenance workers, and in the transportation field they count only those transit drivers employed by a municipality. These data reveal that government workers have remained a roughly constant fraction of the civilian labour force. In 1961, we devoted about 10 percent of our manpower to managing government and in 1974, 12 percent (Table 4, Appendix).

It is clear that the principal explanation for the growth of government spending, and the increased relative position of government in our economy,

has been the growth of government transfer expenditures. The ratio of transfers to gross national product has risen to 0.17 in 1975 from 0.08 in 1951 (Table 1, Appendix).

One final measure should be provided in any summary description of government spending in a federal country such as Canada: the spending by level of government. Considering government activity with respect to the provision of public goods and services, the provincial and local sectors now represent 76 percent of the government sector. In the early 1950s they represented only about 49 percent. The provincial sector has grown most rapidly, from about 18 percent to 42 percent of the government sector. In Ontario, provincial spending to produce public services has risen from about 7 percent of gross provincial product to over 17 percent (Tables 2 and 5, Appendix).

Government transfer activity reveals a different pattern. The local government sector provides almost no cash transfers. The provincial sector provided about 22 percent of the transfers in the 1950s and now provides about 30 percent. In this most rapidly expanding area, the two senior levels of government have behaved in roughly the same fashion (Table 3, Appendix).

The general picture which emerges from these measures can now be summarized. Government spending has increased dramatically as a fraction of national product. This expansion resulted mainly from a growth of transfer payments rather than an increasing proportion of our output being devoted to public services. The rapid expansion of health and education in provincial spending has been accompanied by a relative decline in other areas, especially at the federal level. It should be emphasized again, however, that these data measure only a part of government activity and none of the effects of government on society. Although no quantitative estimates are available, there seems little doubt that government involvement in the economy and society by means of tax expenditures (tax concessions) and regulation has increased dramatically in recent years.

Consider now examples of each of the types of disagreement which seem to hinder the establishment of rules which would guide public sector decisions.

Government and Individual Liberty

"Liberty" is an oft-used word. Its meaning seems perfectly clear until one tries to define it precisely. Like the word "love", it means so many things to different individuals and, indeed, means different things to the same person depending upon time and circumstance. But the ambiguity of the meaning of liberty does not make the concept any less important.

In the context of the role of government the concept of liberty (or freedom) usually is thought to include two dimensions: diversity and individual rights. These will be considered in turn.

Some government activities undoubtedly maintain our freedoms; the enforcement of the laws governing personal safety is the most obvious example. But beyond this floor, to which all of us can agree, there is an enormous scope for controversy.

It is frequently argued that when governments take on a role greater than the maintenance of personal safety, they reduce our freedom. This is to say, they reduce the range of choices available to individuals. By definition, when some kinds of goods and services are supplied by governments, individuals cannot choose either the quantity or quality of those goods and services that they desire. For example, the individual cannot choose to have less police protection, a lower quality educational system or less national defence even though such decisions would give him more money to spend on privately consumed goods or services. In contrast, the decentralized private sector, it is often argued, not only permits each individual to choose the kinds, quantities and qualities of the goods and services that suits his or her tastes but also, through competition, generates a greater diversity of goods and services than the public sector could ever do.

Others argue the antithesis: they believe that larger governments can and do expand the range of individual choice and encourage diversity. It is argued that private markets are not well adapted to providing those types of goods and services for which a price for each unit consumed cannot be charged because those who do not pay cannot be excluded from their enjoyment. There are, after all, goods and services that provide benefits that are not confined solely to those who directly consume them. Police protection, public health, regional planning, a civic convention centre and a community hockey arena have these characteristics. It is also argued that governments increase diversity by such activities as underwriting business and university research costs, by supporting the arts and by supporting agencies, such as the Canadian Broadcasting Corporation, that provide alternatives to private sector agencies.

The concept of liberty – freedom of choice – also encompasses individual rights or, in more formal terms, the sanctioned relationships among people and the rules governing ownership and use of real and personal property. Again the issues are subtle and illusive. There are eloquent proponents of alternative points of view. The debate goes on at a philosophic level, encompassing such grand ideas as theories of pluralism, and at the most mundane level, encompassing the actual regulations which can govern matters down to whether or not dogs should be allowed to relieve themselves in public parks.

There are those who argue that we are losing our freedom through exces-

sive government rules and regulations and bureaucratic red tape. There are others who argue that governments, by more stringently defining the rights of some, have expanded the rights of others. As a nation becomes more urbanized and industrialized the likelihood increases that the behaviour of one individual will affect the well-being of others. The fact that pure air, water and soil are not inexhaustible resources has been increasingly recognized and has led to public intervention. The restriction against my burning leaves in my backyard is an expansion of my neighbours' right to clean air.

From the political theoretic perspective the argument is that a balance is needed between political and economic power. The proponents of this viewpoint argue that a growing government share of national income destroys this balance. This group believes that once government spending reaches a certain percentage of total output governments indirectly control, or at least dominate, society: each individual becomes dependent upon the state for the achievement of his or her goals. The increasing role of the government, it is thought, means that the usual checks on its power gradually disappear.

Also, some hold the view that beyond a point (which is rarely defined precisely) governments cannot be controlled by elected representatives: the civil service becomes self-perpetuating, self-regulating and self-aggrandizing.

Another group takes the view that a balance among conflicting power groups in society is necessary. From this perspective governments have had to become relatively larger because other groups have become relatively stronger. Organized labour may be able to shut down essential industries. The media now seem to be dominated by the voices of a few. A handful of corporations have cash flows greater than the governments with which they negotiate. A strong government sector, it is argued, is required to arbitrate the conflicts between these powerful groups and press the collective interests of the rest of us. But there is always some ambiguity in these arguments as to whether a strong government, looked upon as a countervailing force, necessitates ever larger government expenditures.

It would be foolish to believe that there is a ready answer to the endless quandary posed about the appropriate role of government in the maintenance of liberty. It is a tightrope over which each generation must walk and try to keep its balance. The Ontario Economic Council is of the view however, that, while not decrying all interventions by governments, the time has come for a pause so that our society can catch its breath and, what is more important, reduce the level of uncertainty which threatens to engulf us because of the constantly changing boundaries of individual rights.

Government and Efficiency

Another example of disagreement about the impact of government on society can be found in discussions of efficiency. Are we using the resources

commanded by the public sector efficiently? Could we have the same programs at less cost? The adjective "efficient" is often used as a synonym for "good" or "desirable". The economist's definition of production efficiency is more narrow. Production is efficient if no more of a desired output can be yielded from the resources being used. Here it will be used in this more narrow sense.

To measure the efficiency of a government program demands a measurement of the output. One cannot claim that fewer resources would produce the same output, or that greater output could come from the same resources, unless one can measure the output in the first place. Management consultants, academics and civil servants have, for many years, attempted to develop measures of the output of some government programs. Progress has been slow in part because data collection is expensive. But there are other factors. To illustrate, consider medical and hospital services. What is the output of a hospital? One might measure patient days or the number of patients treated or the number of doctors' hours used. The list could be lengthy. None, however, would measure output.

The output of a medical facility is the increase in health (or the decline in illness) which occurs. How does one measure the degree of health? How does one value the saved life of a baby or the reduced discomfort of a kidney patient? How does one estimate what would have been the health of those living in the community in the absence of the hospital?

One should not, however, be too pessimistic – many measures of government output and efficiency can be developed. Many functions of government can be measured, including such things as construction of buildings, dispensing cheques, information processing or water purification. Even in the health care area, operational output measures are being developed.[2] By comparing the real cost per unit of output over time, or between the public and private sector, or between public bodies in different jurisdictions, estimates of efficiency may be developed. Investment in further research in this area would likely be fruitful.

Perhaps it is because the output of government is so difficult to measure that we hear such divergent opinions about its efficiency. The existence of the controversy is not surprising. Many activities are carried out by governments precisely because the value of their outputs is not amenable to measurement and therefore their prices indeterminate.

This inability of analysts to develop operational measures of output for some government programs seems to have had serious repercussions. In the period since the Second World War numerous reforms have been instituted to improve management in the public sector. One of the most fundamental of these reforms was replacement of the "line-by-line" system of government expenditure examination with a Program Planning and Budgeting System (PPBS). PPBS took different forms in different jurisdictions. But the thrust

was the same. The old system which emphasized a comparison of this year's expenditure, for example on pencils, against last year's was replaced by a system which purportedly weighted the program's achievements (the value of the output of the program) against its costs. Adoption of PPBS was analogous to the adoption as a decision rule of the rate of return calculation used in the private sector.

There are few who would assert that the management of government programs was significantly improved by the adoption of PPBS. There are many reasons for its limited success. But of great importance is the fact that PPBS requires measures of government output (i.e. program effects). The old system dealt with the costs of inputs and largely ignored the important questions of the yields from the inputs. The new system has asked the right questions but has been incapable of supplying persuasive answers. The result seems to have been a loss of control and accountability within governments as the recent report of the Auditor General of the Government of Canada suggests.

No one would argue that the major government initiatives of the past several decades would have been greatly affected had PPBS not been adopted. However it is probably true that in the public service the concept that "the manager should manage" was extremely naive. It did not take into account the problem of ensuring accountability when there is no "bottom line": the test of profitability.

The efficiency of government programs in the areas of health, education, housing and social security was considered in papers published by the Ontario Economic Council in March 1976. In many instances it is evident that the goals and objectives of programs could have been achieved using considerably fewer resources. Many of our social security and housing programs were initiated to assist the poor but gave benefits to middle and upper income households. Large transfer programs have had, apparently, little influence on the distribution of income. The cost-sharing arrangements that existed between the federal and provincial governments discouraged, for example, medical manpower substitution and the use of lower cost alternatives to hospitals.

The examination of many government programs reveals perverse incentives. Some community colleges and universities provide programs that bestow many benefits on the individual but few on the community. Yet the programs are paid for by the community. The fee-for-service system, coupled with Medicare, encourages doctors to provide more medical services than are required. The social welfare system discourages work for some kinds of beneficiaries. Duplication, and an ambiguous locus of responsibility (especially between the provinces and the federal government) has characterized too many programs.

The Council continues to support the analytic framework developed in

its earlier papers and refers the reader to them for an elaboration of the kinds of issues just raised.

However, analytic discussions of government efficiency, although vitally important in the development and execution of sound programs, do not seem to capture the essence of public discontent. To say that a program designed to help the poor is inefficient because it gives many benefits to the non-poor seldom raises public indignation. Public discontent seems to be more a result of such things as the *perception* that civil servants are overpaid or that government welfare programs support the undeserving and lazy (although they may be poor). Over-utilization of the health care system, costing hundreds of millions of dollars, provokes little outrage compared to revelations of exotic trips at public expense, or that the gross incomes of doctors are larger than our own!

In dollar terms, many of the items which attract public ire are insignificant. The incongruity probably arises not because the analysis of the cost effectiveness of government programs is too arcane, but rather, because the discontent is concerned with the relative income and status of individuals in our society rather than inefficiency and waste. The relative positions of public servants, teachers, hospital workers are perceived by many to have improved in the last decade. The reaction is apparent. Conceivably what is required is to weed out the least competent and pay the most competent public servants, teachers and doctors more. But this alternative is rarely discussed. Relative positions seem more at the heart of the issue.

Another dimension of the efficiency debate concerns the impact of government on the efficiency of the private sector. These effects are especially difficult to measure and certainly there is no institution inside or outside government attempting to assess them systematically. As noted earlier, the Ontario Economic Council feels strongly that these effects, especially the effects of regulation, deserve closer scrutiny. A companion paper entitled *The Ontario Economy to 1987* discusses some of these issues in greater detail.

Government and a Just Distribution of Income

The problem of establishing rules to define the public interest is frequently complicated as one attempts to make a general goal more specific. For example, all seem to agree that governments should work to secure a just distribution of income – but what is a just distribution?

The dilemma of defining a just distribution is confronted in considering almost every conceivable government action. Indeed many government programs have as their stated goal a change in the distribution of the output of

our society. In recent years governments have been particularly concerned about how incomes are distributed in general and about the distribution of housing, health care and education in particular. There has been an enormous concern with what might be called "distributive justice". The passion for greater distributive justice probably has been one of more significant social forces during the last several decades in Canada.

The rapid rate of economic growth in the 1950s and 1960s offered great potential for redistribution. Each slice of the pie could grow, but the smaller slices might have grown more rapidly. The scene changed dramatically in the 1970s: energy scarcity and environmental concerns have made continued rapid economic growth less likely and, in the minds of some, undesirable. The recent recession and antipathy toward the growth of government spending have meant that fewer funds are available for new or expanded programs or increased transfer payments. The desire for an even greater redistribution of income and of social status has not been abandoned. Indeed it has probably intensified with a more slowly growing pie.

The issue of distribution is important not just in considering programs which explicitly transfer income. Governments change the distribution of wealth, income and well-being in many ways.[3] Some are direct, such as raising money through the tax system, distributing the revenues as transfer payments and by providing public services. Others are indirect, through changing wage rates, interest rates, prices, unemployment rates and growth rates. Almost every act of government involves such indirect changes. Unfortunately, relatively less is known about the indirect effects of government policies on income and wealth redistribution. The Council has recently sponsored research in this area. Although no final results are now available, one may tentatively assert that the indirect redistribution effects may be at least as significant as the direct.

Given the importance of distributive issues it is remarkable how few attempts have been made to make specific the concept of a just distribution of income. Perhaps it is because we all realize that any specific proposal would not command widespread support. How much should a doctor earn as compared to a lawyer, a steelworker or a street sweeper? Should there be differences due to training, native ability, and personal risk or social prestige associated with a job? Should society permit differences to exist because people decide differently regarding education, regarding leisure and work, and regarding consumption and investment? Should a hard-working parsimonious couple be allowed to bequeath a large estate to their children? The list of such questions could go on and on. Different answers to each question would be offered by different people. Even if it assumed that society has little interest in the distribution of income but wishes to ensure that all have sufficient income for a decent existence, another list of questions arises. Should support to the employable and the unemployable be the same?

Should support be offered to students, to single parents with young children, to single parents with adolescent children?

Individuals are virtually unanimous in the belief that society ought to have a just distribution of income. They also seem to agree that the present degree of inequality in the distribution of income and wealth should be reduced – except, and it is a big exception, when they *perceive* that a policy change designed to achieve any one or all of these objectives, would, or conceivably could, reduce their relative income, wealth or social status. Apparently individuals love virtue, or the appearance of virtue, when it is its own reward and is likely to cost them very little.

Individuals support the principle of a more equal distribution of income. But then they oppose programs which reduce their own relative well-being and strongly support programs offering offsetting government benefits to them.

In the context of discussing governments and a just distribution of income one remarkable fact needs to be remembered. Despite all the furor about unemployment insurance abuse, rising welfare payments and "corporate welfare bums", the distribution of money income in Ontario and Canada apparently has remained remarkably stable over the past fifteen years.[4] The constancy of the relative shares of money income (where income includes all transfer payments such as welfare, old age security payments and family allowances) is startling in view of the widespread feeling that the better off have been giving vast amounts to those less well off and in view of the indisputable growth of transfer payments.

A number of explanations of this paradox – our perceptions of the enormous expansion of government on the one hand and the apparent constancy of the relative shares of income on the other – are possible.

An obvious possibility is that the data used to measure the distribution of income are faulty. It is known, for example, that certain types of income are under-reported and that other types are not included at all such as some capital gains and virtually all income-in-kind. Nevertheless, attempts to correct these omissions have not revealed significant changes over time and a rather more unequal distribution of income at any point in time.

It may be that our perceptions of the social security system do not conform to the realities. Frequently we forget how many of the poor, or those with very low incomes, are ineligible for benefits (for example the so-called working poor) or do not receive benefits from the available programs. Furthermore, the gross expenditure on many of the transfer programs may give a false impression of the extent of the redistribution they achieve. Some programs provide universal coverage and many of the payments flow to the relatively wealthy.

Another possible explanation is that, in the absence of government transfers, the distribution of income would have become more unequal, largely

because of demographic factors. Perhaps government programs have simply maintained the relative distribution pattern that would otherwise have become much more unequal.

Alternatively, perhaps governments cannot change the relative shares of the pie. Attempts to take from the haves in order to give to the have-nots perhaps have resulted in counteracting moves on the part of the haves, either through exploiting market power or securing offsetting benefits from government. If this were the valid explanation, the net result would be a constancy of income shares. While this hypothesis is not likely a complete explanation, the reaction of those who have borne the cost of redistribution (or more importantly those who perceive themselves to have borne the cost) cannot be ignored. The sequence of policy change, perceived burden, reaction, and offsetting policy change seems to be a central dynamic at present in society.

Finally, it must be recognized that changes in the measured distribution of money income do not take into account the full impact of government on economic well-being. Two additional factors are missed in only measuring income. First, the impact of the tax system is ignored. It is after-tax income, not gross income, which is indicative of relative well-being. Second, the imputed value of government services received by individuals also should be included in the calculation. Many of the largest government programs provide significant quantities of public services to low income individuals and families but are ignored in the arithmetic.

Making estimates of the distrubution of income that take these factors into account is extraordinarily difficult from an analytical point of view. A number of studies have recently been published[5] which indicate that the overall impact of taxation, transfers and expenditures is a moderate redistribution of net benefits from upper to lower income groups. However, the one comparison which has been made between the net effect of government taxation and expenditures at two points in time does not show that the net effect of these policies has become more redistributive over time.[6]

Conflicts and Trade-offs

Probably the most fundamental source of disagreement is not that we cannot agree about how a government action will influence society, or that we cannot agree about the specific definition of a general goal, but rather that we cannot agree what trade-offs should be made between the various goals.

Many of our enunciated goals are in some sense competitive – a government action to more nearly achieve one will imply a greater distance from another. Almost any program, however small, produces a myriad of effects

some of which will be judged to be detrimental and others beneficial. Restrictions on emissions from mines or pulp mills to secure a more protected environment may mean reduced economic growth and less employment. Restrictions on certain types of foreign investment to gain greater control of our economy may mean fewer job opportunities for Canadians. Increased taxes to secure a more equal distribution of income and wealth may mean a reduction in work effort and economic growth. Restrictions on land use to secure a pleasant neighbourhood environment may mean a reduction in personal freedom.

Even in cases where there is not an evident conflict among the results of a program, there is an implicit competition among goals. If a government action requires resources, time or effort to achieve a goal, they are not available for use in other pursuits whether public or private.

An assessment of a government program requires an assessment of alternatives. The point may seem rather obvious but it is often ignored, especially by proponents of more government or less government. For instance, members of the former group often argue that if there are negative spill-over effects (a burden imposed on others) from some private activity governments should set up regulations to prohibit it. But the costs of monitoring and policing the regulated activity may outweigh the costs of the negative spill-over. Unfortunately, this kind of comparison is rarely made. On the other hand, members of the latter group sometimes argue that if there is a regulated industry it should be de-regulated almost as a matter of principle and fail to recognize that, in the absence of the regulation, some policy goals would be far more costly to attain.

The previous pages have been devoted to examples of why it is so difficult to develop a definition of what the government ought to do – to develop a definition of "the public interest". So often when a specific policy is discussed the ritualistic acceptance of broad objectives dissolves into rancor and dispute. Even if there were a consensus about what needed to be done, attitudes about the appropriate level of government to act would be constantly shifting.

The existence of the controversies suggests that the mechanism through which we collectively decide about the kind and scope of government activities – the political process – must play a critical role. No government can simply carry out "the public interest" in the light of a few vague statements of objectives. Rather, every government must conciliate the conflicting interests of individuals and groups, each of which have different opinions of what the government ought to do.

The extent of the disagreement among individuals and groups about the appropriate role for government has admittedly been somewhat overstated in the previous pages. On some occasions the consensus about broad goals can be transferred into a consensus on specific actions.

In each of the areas of disagreement discussed in the examples there also exists some consensus. Research and analysis have and will continue to provide estimates of the impact of government which command general acceptance. Many disagreements concerning government's impact result not from different interpretations of reality but from lack of data and analysis. Further work will reduce the disagreement.

The problem of making specific a general goal sometimes does not hinder broad acceptance of specific proposals. Although the precise specification of a just distribution may be contentious, people seem quite willing to accept the principle that less rather than more equality is desirable provided only small changes are contemplated. There seems to be a willingness to accept rather rough and ready guidelines. Certainly one may suffer under such an approach but this may be less costly than endlessly wrangling to make all goals absolutely specific.

Some trade-offs among competing goals are widely accepted. Most accept the restriction on liberty represented by seat belt laws and speed limits when compensated by increased personal safety and reduced public health expenditures. Most accept the forced closure of plants which pollute irrevocably the adjacent river system (often the employees are also those who suffer the worst effects of the pollution).

Undoubtedly, as well, there is a role for political leadership: the art of informing and persuading and demonstrating by good example. The views of voters are not cast in concrete, at least not *all* of their particular views on particular issues at any particular point in time. Complete consensus is never possible: greater consensus can be attained. We cannot dwell here on the role of political leadership as vital (and as rare) as it may be. The question is perhaps too subtle. Certainly what is involved is not well understood in any formal sense.

The intent in citing the examples of disagreement was not to argue that every individual is in complete opposition to every other individual, every group in disagreement with every other group. Rather the intent was to argue that criteria to govern government activities are extremely difficult to develop. The notion of "the public interest" is extremely imprecise. There exist fundamental disagreements among people in the country, the province and urban areas which must be resolved through the political process. An understanding of the decision-making process of government and of how it reconciles these differences is vital to an understanding of the role of government. The next chapter attempts to offer some insights into this reconciliation/conciliation process.

3
The Decision-Making Process

An Alternative Approach

The determinants of the relative size and composition of the public sector have been studied much more intensively in recent years than they were for decades, particularly by a group of public finance economists who have applied the conceptual model of economics to the political decision-making process.

Previous analyses placed far less emphasis on the decision process, seeing the demands of citizens as the principal determinant of public activity. Increases in incomes were considered to mean an increasing demand for public services. The programs of governments were seen as similar to luxury goods: as incomes rose we were willing to spend an increasing fraction of our resources on government programs.

Changes in the age distribution of the population were felt to be an important factor in rising demands. The baby boom of the 1950s caused increased expenditures on education (primary, secondary, universities and community colleges). The commitment of real resources per student was held relatively constant so that the public sector share increased as the demographic bubble arising from the baby boom gradually aged. Similar patterns in the housing and medical care areas can be found.

Frequently the relatively higher rate of labour productivity growth in the private sector is cited to explain a growing public sector. Labour productivity growth resulting from the use of new or more capital equipment can permit wages to rise without increasing prices. Many of the services provided by government are labour intensive, and unlikely to experience cost reducing

technical changes or permit significant substitution of capital for labour. The pattern of wage increases seems to be similar because of competition between sectors. Therefore, it has been argued, to maintain government real output as a constant fraction of total real output the fraction of nominal output going to the production of the public sector necessarily rises.

Certain basic changes in society, it is also argued, have meant a shift in how we choose to divide our resources between the public and private sectors. Urbanization has meant that services more efficiently provided privately in low density settlements in the past (such as fire protection, sewage disposal and water) are now more efficiently provided collectively. Automobiles, airplanes and snowmobiles and certain industrial processes using new chemicals, appear to have direct and indirect adverse effects on the well-being of others. These negative spillovers often require regulation. Laws and regulations must be drafted and police and enforcement systems established. Certain changes in our society have made the provision of a constant level of service more costly. With less reading done in the home the achievement of a minimum literacy level becomes more costly; with a declining respect for authority, the maintenance of a given level of public safety also becomes more costly. The optimum mix of public and private goods seems to be shifting.

These analyses of the determinants of government spending have contributed to an improved understanding of what has been happening. But there is an interesting alternative approach to the study of government policy which has received less attention. This alternative approach places emphasis on how the demands of citizens are translated into government policy decisions, as distinct from the other approach which emphasizes how these demands were determined and assumes they would be implemented. The alternative approach assumes that demands are given and considers by whom and how they are voiced, and by whom and how decisions are reached. The emphasis is on the decision-making process as such and how the structure of the institutions and rules of the process mold the outcome.[7]

The political and bureaucratic systems of our country can be viewed as institutions for making decisions, just as private markets are institutions for making decisions. Economists have, in the past, examined the effects of private monopolies and government regulation of business in an attempt to ascertain whether changes could be made to ensure that the well-being of individuals could be enhanced. Similarly, government institutions can be assessed in order to determine whether or not their decisions reflect the preferences of the electorate.

This alternative approach begins from the presumption that, for the purpose of analysis, politicians, interest group leaders, journalists, voters and government officials all act in their self-interest: they make decisions to maintain and preferably improve their own well-being. The institutional

structures are investigated within which each of these groups operate: each group has its own set of rules which constitute the incentives and disincentives for the members of the particular group. Looking at decision-making in this way provides some insights into the policy outcomes.

This approach represents an extension to political decision-making of the approach used by economists to analyse decisions in the market place – the decisions of consumers about what to buy and the decisions of firms about what to produce. The behaviour of politicians, government officials, interest group leaders and journalists is analysed as one would analyse the decisions of the labourer or the consumer or the businessman. All are human, all make their decisions in light of the prevailing rules and in the search for greater satisfaction. The explanation behind the different behaviour of the members of these groups is to be found, at least in part, in the different rules (incentives) which apply to the several groups and in part in the skills and attitudes which the groups require in recruiting their members. The explanation does *not* lie in differences in the relative selfishness of the members of the groups.

This approach to policy analysis may seem at first nihilistic and cynical. Heretofore the analysis of government has usually sought to find the efficient or "morally valid" policy and, by implication, has assumed that politicians and civil servants (and the other groups involved) are constantly searching for "ideal" policies. The approach adopted here does not deny the possibility that morally correct or efficient policies are sought: rather it does not assume, *a priori*, that this is the shared objective of the groups. The question to be pursued is whether or not the decision-making rules of the several relevant groups tend to produce efficient and equitable policies. The approach will also be judged in terms of its predictive or explanatory power.

It is interesting to note that this method of analysing decision-making is now being applied to non-profit institutions, clubs, corporations and even socialist organizations. In these analyses it is no longer assumed that, for example, a corporate manager makes his decisions to maximize the profits of a firm. Rather it is assumed that the manager makes his decisions to maximize his self-interest. The analytic question is to determine under which incentive system the self-interest of the manager is consistent with profit maximization for the firm. For then, and usually only then, is the manager likely to make decisions that are consistent with the shareholders' interests.

Politicians and Voters

The purpose of this section is to suggest how the approach discussed above can be used to analyse our system of representative government. As suggested earlier, the most controversial dimension of this approach is the

assumption that individual behaviour is motivated by self-interest. The electoral process can be seen as a means by which politicians, political parties (and those that support them) seek to attain or retain office.

Politicians are not considered to seek office in order to promote their conception of "the public interest" or to carry out particular policies. It is assumed that politicians, like other individuals, are motivated by the gains, tangible and intangible, which flow from the holding of office. These gains include money income and perquisites, personal satisfaction from exercising power, prestige in the community, and the acquisition of skills and information which may be useful either in obtaining subsequent employment in a non-political job or in performing more effectively during a second term of office. Of these payoffs the satisfaction gained by the exercise of power, in particular to achieve what the politician believes to be "right", is probably paramount.

Individuals as citizens are also motivated by self-interest. They are presented with choices among candidates and the platforms of the political parties which they represent. The promised actions of a candidate (or more correctly the actions it is anticipated he or she will carry out) usually involve both costs and benefits to the voter. The costs comprise, in the main, the share of the taxes which the voter will have to bear but they can also include the hidden costs of public regulation or public spending not approved by the voter. Benefits are similar. There can be benefits to the individual voter from specific expenditures, regulations, a well-managed economy and from transfer payments to others whom the voter considers deserving. The voter will usually support that candidate whose anticipated actions are expected to yield the greatest net benefit as he or she sees it at the time.

Models using the assumption of self-interest will not of course be able to explain all government decisions; the test of the worth of these models will rest on their ability to explain and predict reality. There exist politicians who seek election to implement programs consistent with their ideological position, or who seek election to implement their vision of an equitable society. If elected, any interest in re-election may be transcended by other goals for such individuals. There also exist voters who support programs against their self-interest. One might argue that this is simply the self-interest of these politicians and voters – politicians who like being leaders rather than elected representatives; voters who like being altruistic. Such an argument, although irrefutable, robs the self-interest postulate of its usefulness. It becomes so general as to encompass everything. Such behaviour is simply not well explained by this model.

It seems, however, that such behaviour is the exception rather than the rule. The widespread use of the government process to achieve partisan goals and to achieve benefits formerly secured through private activities suggests that to say politicians make decisions according to "the public interest" and

that voters support parties whom they believe best able to discern "the common good", is too narrow a view.

Self-interested politicians and voters will interact in any number of ways. One of the principal determinants of the outcome will be the rules under which elections take place.

Consider the simplest world of citizens directly voting on one issue, for example education. There are three choices available to them: one with a large budget, one with a medium budget and one with a small budget. The alternative supported by a majority of voters, when any two are compared, is selected. In making their decisions the voters consider the net benefits to them of each proposal, which involves balancing their perceived share of increased taxes against their perceived share of educational benefits. The chosen proposal probably will be the one which contains that educational program which appeals to the median voter.[8] The median voter, by definition, has preferences such that 50 percent of the population favour a larger education budget and 50 percent favour a lower budget. That the choice will correspond to that held by the median voter can be easily demonstrated: if any alternative proposal were advanced which was not the median it could be beaten by another which was slightly closer to the middle.

Different outcomes are likely if the rules of the political process were different. Suppose that the decision rule of unanimity (rather than majority) were in effect. Far fewer measures would be passed in such a legislative process for each elected representative would have a veto. Suppose that a two-thirds majority were necessary to approve the educational program, in this case one could not assert that the preference of the median voter is likely to be selected. Alternatively, suppose each eligible individual were required to vote not for one program but for all programs in order of his or her preference or for all programs weighted by the intensity of those preferences. The list of alternative voting systems is endless and the results, under each, in terms of elected candidates and executed government policies probably, would be very different. We have become so accustomed to the existing electoral process that we tend to treat it as inexorable. The reality is that there are a multitude of alternatives and that each of them would, in all likelihood, yield different decisions.

The actual political process is, of course, more complex than this simple example. In every election there are hundreds of issues to be decided. But voters can only vote for one man to decide on the policy bundle. Voters do not simply vote on single issues, but are forced to support a candidate and, in all but local elections, usually a candidate who represents a particular party. The example does suggest, however, how the rules of the political process may influence the selection of programs.

The existence of numerous issues of unequal interest to voters often leads to a phenomenon called "logrolling" or "vote trading". Legislators,

when voting on a particular bill often agree to support something about which they care relatively little in return for support on something about which they care a great deal. Many commentators imply that the process is dishonest or at least dishonourable. Pejorative terms such as "the collection of I.O.U.'s" or "backroom deals" are often used to describe what is going on. Logrolling does not deserve to be treated in derogatory terms. It is a part of the political process and often contributes to the effective functioning of a democracy. Implicitly, all voters engage in logrolling when they support the platform of a party: few, after all, support every single item of a party platform. But in order to secure the policies about which they feel strongly they accept those which they do not like but about which they feel less intensely – in effect they trade more of the "good" for less of the "bad".

The process of logrolling is necessary to secure the passage of many programs whose benefits may outweigh the costs, but whose benefits are not distributed widely. Consider, for example, the provision by the Province of Ontario of a proposed park near Sudbury where the benefits clearly outweigh the costs. If the park were to require majority support in the legislature it probably would not be approved. Members, except those representing Sudbury and contiguous areas, would not support an expenditure which would raise the taxes of their constituents but offer them few if any benefits. However, with logrolling, either implicit or explicit, the park may be approved. Members from other regions may support a project which will cost them little and in return expect the support of other members for projects or programs of great benefit to them (perhaps a park in their region or assistance in aiding a constituent).

The existence of logrolling demands that one be extremely cautious in considering who benefits from one program in isolation from all others. Considered alone, a program of benefit to mink farmers may seem an outrageous gift to a special interest group. But when considered in conjunction with other projects and programs it may appear that the net benefits of the bundle are much more widely and evenly distributed. Programs of benefit to the wealthy may be necessary to insure the passage of programs to redistribute income to the poor.

It is sometimes argued that logrolling leads to an over-expansion of the public sector. Consider, as a simple example,[9] a hypothetical program placed before the one hundred and twenty-five members of the Ontario legislature. The cost of the program to the Province is estimated to be $125 and is to be borne equally by all constituencies. The benefits to the citizens of one constituency are estimated to be $80 with no benefits to citizens of other constituencies. From the viewpoint of the province such a program should not be supported for the costs are clearly greater than the benefits. However if 63 of such kinds of programs existed, a majority coalition could ensure

passage of each of them because the net benefit to each member of the coalition would be $17. The *net* cost to the Province of this coalition would be 63 times $45 (the net cost to the Province of each program), or $2,835!

It should be pointed out that this over-supply hypothesis can apply in the situation of majority rule with no logrolling – if benefits can be concentrated and the costs spread across the entire population. A program which yields a group of 63 constituencies a total benefit of over $63 will be supported. But unless the benefits are over $125 the support leads to over-supply – a program is adopted whose costs exceed benefits.

Another characteristic of our political system which has a particularly important impact on the decisions which are taken is the lack of information. Politicians do not have complete information about the preferences of voters or on the impact of proposed policies. Voters do not have complete information on the platforms of the candidates and parties and the relevant information is costly to acquire in time and/or money terms. This almost trivial fact – that information is not complete or free – seems to explain many facets of the political process.

This raises the question of the extremely important and complicated role of the media in the decision-making process. To a degree, newspapers, private radio and television stations, and magazines can be looked upon as any other business. The owners seek to make an adequate return on their investment; and the news, and other programs, can be looked upon as the vehicle by which they seek advertisements. Advertising revenues depend upon the number of readers, viewers and listeners the particular program or publication reaches. Media businesses can not afford to adopt, on a large scale, standards that are inconsistent with public tastes. This sometimes encourages dissemination of the sensational and superficial which apparently has a much wider market than the balanced and the thoughtful. Like any other pressure group, the media often wants government involvement that would increase the net revenues from their respective business enterprises.

The incentive system within the media can have a significant influence on the flows of information between voters, and between politicians and voters. Journalists are under great pressure to produce materials that indirectly sell the advertisers' products. Politicians are under pressure to provide news in a form that is likely to appeal to journalists. Politicians often enter logrolling relationships with the media where, although the agreements are presumably unexpressed, "scoops" on some issues provided by the politicians are exchanged for silence on the part of journalists on embarrassing issues. These are, however, likely to be precarious bargains because the time horizon of the journalist is even shorter than that of the politician. The former have to deliver every day or week or month. The latter usually have a number of years to assemble the most attractive package to offer voters. Politicians are often put in the position where trivial errors become devas-

tating while major, quiet successes (or failures for that matter) are not reported to the public. This is not to suggest that any form of media censorship would be appropriate: far from it. Rather, it is to point out that the incentives prevailing in the media are not unrelated to the information the public obtains *and* to the behaviour of politicians.

As a result of the fact that information is costly, voters tend to inform themselves only about those issues which directly and significantly affect them. To do otherwise would be more expensive than the potential benefits warrant. As a result, voters often develop convenient shorthand methods of assessing the worth of a candidate: perhaps his ideology or perhaps his style or some other simple characteristic such as religious affiliation, mother tongue or political party. The often criticized ignorance of many voters may represent the result of perfectly rational decisions reflecting the fact that information is costly to obtain.

Politicians similarly face difficulties in obtaining information. The impact of government actions on our economy and our society is often only known imprecisely. Without such knowledge the politician has difficulty in preparing a package of programs which reflect the preferences of the electorate. We all wish to reduce regional disparities; but what will lead companies to locate in slow-growth regions and what will be the impact of relocations on other regions of the country? Devoting manpower to the investigation of government programs and of alternative approaches will frequently be a worthwhile investment for a politician, and for that matter, for the voters.

The other requirement in the political matching of programs and votes is to know the preferences of voters. Again, information is far from complete, and costly to obtain. The politician has many avenues open to ascertain the voters' preferences – from living and visiting in his riding, to conducting opinion polls, to listening to the media. Frequently groups of persons who feel intensely about an issue proclaim their preferences loudly and often, in the hope that volume and frequency will be interpreted as numbers. In the end it is the political skills of the elected representative – the requirement for his job – which must be relied upon to gauge voter preferences.

Interest Groups

Frequently voters find it is worthwhile to hire representatives to keep informed about the decisions of government and to make representations on their behalf to the decision-makers. These interest groups or lobby groups may represent a geographic area, such as ratepayers groups, a single profession, such as the Ontario Medical Association, the companies of one indus-

try, such as the Urban Development Institute, or even a group of people interested in a particular policy problem such as the Ontario Welfare Council.

The behavioural assumption – self-interest maximization – which was used to explain the choices of voters can also be used to explain the formation of interest groups. Where there are a number of people who share a common interest, the possibility of forming a group exists.

The common interest must, however, be of a special sort. Usually the interest cannot be pursued individually or is far more expensive individually. It might be that something cannot be bought in small quantities so people come together and share in its purchase and use as in the formation of a golf club; it may be that a coalition of people is necessary for the interest to be realized as with a social club or tennis club. Of most importance to understanding the formation of groups sharing a common interest in securing a change in government policy is the spillovers which result if their interests are realized.

Suppose one individual managed to secure a concession from government: for example, if one clothing manufacturer persuaded the government to impose a quota on clothing imports. All other clothing manufacturers would enjoy the benefits of the concession. In most cases, the benefits from the change which flow to *one* individual do not equal the *total* costs necessary to secure the change through lobbying. If, however, the *total* benefits to the group exceed the total cost to the group it pays the individuals to coalesce in order to secure the policy changes that serve their common interests (provided the costs of organizing do not eat up the net benefits).

Although spillovers provide a rationale for the formation of certain groups they also explain the difficulty in keeping groups together. Because the benefits of a successful lobbying effort accrue to everyone, not just those who have borne some of the costs, individuals of like interest have an incentive not to join the group if they think it will continue to exist and be equally effective in the pursuit of their interest without their participation. They can then enjoy the benefits and bear none of the cost. Individuals, in other words, have an incentive to feign disinterest in the pressure group. Rather aptly, this phenomenon is called the "free rider" problem.

Small groups are less likely to suffer from the free rider problem. In small groups it is more probable that if one member withdraws the entire group will cease to exist because the contribution of each member is more likely to be necessary. There is no incentive to be a free rider. Alternatively, even if the group would continue to exist without one member, the remaining members are easily able to identify the free rider and apply social pressure. The Shady Grove Cottage Owners Association is likely to be a strong cohesive group when lobbying to oppose the widening of the lakefront road. The Drivers on the Lakefront Road Society is unlikely to be a cohesive

group; unlikely to make a very strong submission in support of the widening. Indeed, the Society is unlikely even to be formed. There are, of course, other groups, in particular the roads department, whose voices will be influential in a decision on road widening.

Small groups are also often strong because the benefits to each member are high in relationship to the organizational and lobbying cost. The container manufacturers are able to organize to oppose legislation requiring returnable bottles, whereas the supporters of such legislation have a great deal of difficulty in organizing because the potential benefits to the individual are so small relative to the costs.

The difficulty in organizing large numbers of people, when each person may only be marginally affected by a policy, but who in total can bear significant costs, to exert their influence in the political process seems to be an inescapable problem confronted by all representative political systems. Yet, it is only through the counterbalance of this large group, frequently the majority, that the influence of special interest groups can be curbed. Perhaps the only solution is to make the legislature more effective by providing more staff support for opposition members and a greater use of critics bringing in outside independent witnesses. A more informed press could also be helpful.

Examination of some large interest groups reveals that they frequently were not formed primarily to perform lobbying functions and that they are able to coerce all who share the common interest into paying dues. These groups have instituted and can enforce rules that overcome the free rider problem confronting large numbers of people who wish to act collectively. Certain labour unions are a case in point. When labour unions operate under closed shop regulations, they are able to ensure that all who benefit from their activities are union members, and hence bear their share of the costs. Although established primarily for collective bargaining rather than lobbying purposes, many labour unions can effectively pressure governments for the policies and programs they want, because they can count on a continuing dues paying membership.

Parenthetically it is interesting to note the political bargaining power of such organizations as the Canadian Labour Congress is probably weakened because it cannot impose compulsory membership on the labour unions that often impose compulsory membership on individual workers.

Many professional associations operate in an environment similar to that of a labour union. They can exclude non-members from practising and establish and enforce codes of behaviour and pricing. This regulatory function is delegated to the professional association by the legislature. While not the original intention, which seems to have been to protect the public from unqualified or unscrupulous practitioners, the effect of the legislation has been to create powerful pressure groups because of the compulsory nature of the membership act.

Debates about the "post-controls society" must take cognizance of these factors which seem to explain the success of some groups as opposed to others. One cannot reduce the power of the professional groups without deciding how certification and discipline might be alternatively handled. One cannot strengthen consumer representation without dealing with the free rider problem.

The conditions underlying the formation of pressure groups are somewhat easier to specify than the influence of such groups on the political process. It is impossible to say how our society would differ, how taxation or expenditures or government regulations would differ, if pressure groups did not exist. The source of influence of a pressure group is ambiguous. Why should politicians seeking only to be re-elected or government officials seeking only to increase their prestige and influence be affected by a pressure group?

A simple voting model explains some of the influence on political decisions exercised by pressure groups. A pressure group seeking a particular concession can argue that unless the concession is granted it will ask its members to vote for the opposition in the next election or to withdraw their campaign contributions (whether in money or time). The politician confronts the clear cost of refusing the concession and the rather diffuse benefits of refusal. If granting the concession is likely to raise public ire, the concession can be designed to make it less visible, as through a change in a regulation, or a tariff increase or a special tax allowance. Such changes, although of great benefit to the interest group, are not recorded as expenditures to the group.

A more subtle form of exchange between interest groups and government officials (and politicians as well) often exists. The currency of the transaction is information and public support. The interest group offers information about peoples' preferences and agrees to support certain government programs; which assists the civil servant in his dealings with other civil servants. In return the civil servant supports the interests of the pressure group within government. Regardless of the currency – voters, dollars, time or information – the exchange can be analysed as a *quid pro quo* among parties each pursuing its self-interest.

Opinions differ widely about the desirability of this process. Some argue that it enhances the democratic process because it brings government decisions closer to the desires of the electorate. Interest groups, it is felt, exist to inform politicians and civil servants, and to inform the members of the decisions of government.

Interest groups often perform the important function of presenting the viewpoints of occupational groups or certain industries, which could not possibly be completely articulated by the elected politicians who represent geographical areas. Labour unions, business associations and professional

associations all provide this function. Discussions of tri-partism or multi-partism are an attempt to institutionalize this process to ensure a balanced representation. Often individuals who are a minority in every constituency can form an interest group to seek influence in proportion to their numbers. The problem is, of course, that no one can speak for *all* labour, or *all* business. There are enormous differences within these groups as well as between them.

Others contend that interest groups subvert the democratic process, making dollars (even through outright bribery, or more frequently through campaign contributions and slick promotional and lobbying presentations) more important than votes. Undoubtably, pressure groups influence the process in both ways. Information flows are greater, but a man with one vote and many dollars is often more influential than a man with one vote and few dollars.

An interesting example of the interaction of interest groups occurs in the conducting of a Royal Commission (or its equivalent). These commissions, generally speaking, appeal to all members of the public to come forward and be heard if they wish to do so.

This is in contrast to the procedures of our judicial system. The courts have long adopted the principle known as *locus standi* – only those directly affected by a decision have a legitimate place before the court. Even though a person might be utterly convinced that a more equitable distribution of wealth would be socially desirable, that person would not have the right to be heard when, for example, a will was in dispute before the court unless he or she were directly and immediately affected by the decision. One rare exception can occur when the judge allows "a friend of the court" to be heard because he is convinced that the traditional adversary process will not bring out some of the relevant facts. The courts essentially take the position that those who do not like the law as it exists should try to have it changed by the legislature, not through the courts.

When the terms of reference of the Royal Commission are broad, as they often are, the range of participants can be equally wide – some who would be directly, immediately and substantially affected if the Commission's recommendations were implemented and some whose interests are remote, seemingly distant and seemingly extremely minor. Should the views of the former not carry more weight than the latter?

Two points need to be made. The Government, in the appointment of the commissioner(s), can select an individual(s) who it believes is likely to give a reasonable balance, as the Government sees it, in response to the views and interests of the contending parties. Secondly, of course, commissions of inquiry make recommendations and do not create legislation. The Government must ultimately take the responsibility for balancing competitive interests.

Government Officials

Government officials can be assumed to act in their self-interest too. The environment in which they work and the rules and incentives which govern their behaviour can be examined to see whether they explain, at least in part, the outcomes of government activity and whether the rules (incentives) might be changed to secure decisions more coincident with the wishes of elected representatives and the electors.

Those who are employed in the departments of government are, to be sure, somewhat different than those who work in small companies or who work on assembly lines or play professional hockey. Different skills (social, physical and mental) are required. However, for the purpose of this analysis, their degree of integrity is assumed to be similar. All are motivated by self-interest. Those things which can increase the well-being of an official include income, prestige, respect, pride in a job well done, perquisites of office, control of patronage and working conditions. The list would be the same for any worker. But the institutional environment of the departments of government seems to produce quite different behavioural patterns.

A department in government has three important characteristics which appear to play critical roles: the revenue of the department does not come from sales of output but rather from an allocation of funds by the legislature; the "owners" of the department cannot appropriate to themselves the excess of revenue over costs; the output of a government department is extremely difficult to measure.

Usually it is extremely difficult to measure the output and hence to judge the efficiency of a government department. A manager will thus have very little incentive to strive to increase the efficiency of his activities – his superior has difficulty in assessing this aspect of his performance (indeed if efficiency cannot be judged, the manager cannot know what changes would improve efficiency). Remedies for this dilemma are, however, difficult to develop. It is precisely because outputs are hard to measure that many activities are undertaken by government. For the same reason that it is difficult to assess the efficiency of the official, so it would be difficult to assess the performance of a private contractor engaged to perform the same task. The constant interaction between politician and government official may be a better form of control and yield greater effectiveness than a government contract given to a private firm to perform the same service.

The incentives which confront a government official often seem to encourage an increase in the size of the department with no attention to costs. Often by increasing the size of the department the official's prestige, perquisites, and control of patronage are also increased. Increasing the size of a department, although making control difficult also seems to ease the tasks of management. It is almost impossible to fire civil servants or to reward them

with raises in pay (relative to others). The only incentive which superiors can offer are promotions. When a department is growing, promotions to award come more rapidly. New personnel are acquired. Incompetent personnel are bypassed. The tasks of management are eased.

The bureaucracy, of course, is not unconstrained. It operates under the legislature and the cabinet, or at the local level under the elected council. One cannot argue, as some commentators have, that the tendency of bureaucracies to expand explains, in and of itself, the growth of government spending, taxing and regulation. The budgets and actions of all departments are approved by the elected representatives.

Do our elected representatives have incentives to constrain the growth of the bureaucracy and encourage its greater efficiency? The incentives seem to act in two ways. If the same output were produced at less cost there would be funds to spend on other programs without raising taxes – a clear benefit to the politician. Reducing the portion of expenditure going to civil service wages and increasing the portion flowing to key voters would also bestow a political gain. Cabinet ministers and senior civil servants therefore have opposing interests to some degree. However, the benefits of increased spending (on bureaucrats or their programs) must be weighed against the likely reaction of voters. When voters do not seem sensitive to tax increases or when new programs can be instituted without increasing taxes, politicians have little incentive to reduce spending. The reverse situation can hold, however, as it appears to hold at the present time in Ontario.

As is well known, there has been a great deal of discussion about the need for more and better policy evaluations – evaluation of prospective policy changes and retrospective evaluations of existing policy. Despite the fact that many policy analysts have been hired by governments the results have been, by and large, disappointing. The lack of effective policy evaluation can, in part, be explained by the incentives and disincentives faced by government officials. Consider the following examples.

Ministers often have little incentive to specify the precise criteria by which policies can be judged, both because quantitative measures of failure are more difficult to evade than general feelings of disquietude and because the "real" objectives of policies are often quite different from the ostensible objectives. The "real" objectives frequently cannot be publicly acknowledged without embarrassment.

Officials in charge of a government department have an incentive to satisfy their Minister rather than find "the truth". While warnings to the Minister of ineffective policies are obviously in order, in many cases the decision has already been made at the Ministerial level and a rationale rather than an appraisal is called for. This, of course, filters down to the subordinates within the department.

The savings that might result from the adoption of more effective poli-

cies rarely if ever accrue to those who discover them. Indeed, more often than not the reverse is the case – smaller budgets, smaller staffs, endless tension and lower departmental morale are likely to be the outcome, at least in the short-run, of improved departmental program efficiency.

Negative results can be suppressed under secrecy provisions. Why bother to undertake studies that are unlikely to be implemented because the results will not be able to arouse public pressure?

Even within the public service secrecy rules can prevail. Analysts are often hamstrung by a lack of data – particularly data in the hands of operating heads in a department. The deputy has an incentive not to alienate those in charge of operating functions in order to satisfy analysts, because the former have the capacity to hurt him more than the latter.

The rule of Ministerial responsibility also has a part to play. Ideally, the central agencies should be involved in the evaluations. But Ministers – pushed by their officials – strive to maintain departmental autonomy.

Ministers, because they are concerned that analysts are often unaware of political constraints and often have their own biases, are reluctant to give much weight to technical evaluations. The time constraints on Ministers also have an effect. Ministers are captured by the problems of the "here and now" and are reluctant to spend time reviewing an evaluation of an existing policy that is not of immediate public concern.

Judging the Outcome

The roles played by the principal participants in the political decision process – the voters and their interest groups, politicians and government officials have been sketched. Within the rules and incentives of our democratic process they determine the role of government. Several important rules (and hence incentives) that impinge upon them have been discussed. The discussion of the decision-making process could, of course, have been considerably complicated. There are conflicts among members of the same party. There are interest group interactions with political parties and the press. There are many levels of government in Canada and international relations that are obviously important. These additional complications affect the outcome. But the essential approach remains. Each group or individual is assumed to be motivated by self-interest and seeks to influence the instruments of government policy.

A full understanding of a policy problem demands that the important groups and their interests be identified, that their reason for seeking to influence a particular instrument be spelled out, that the incentives operating

on each of the groups be identified and that the rules for reaching a decision be defined. This framework will be applied to four specific policy problems in the following chapter.

At a general level, an attempt can be made to judge the decision-making process. One must however be very cautious. The "public interest" cannot be simply and objectively defined. Too often criticism of the outcome of the government decision-making process is no more than an assertion of our own value judgements about who the gainers and losers should be. This paper has tried to avoid such proclamations. It is clear, however, that some criteria to permit assessments can be developed.

One can assess the decision-making system by whether the outcome reflects the wishes of the electorate. Establishing what bundle of programs reflects "the wishes of the electorate" is in some sense arbitrary – one could claim that only the bundle which had unanimous support correctly reflected the wishes, or that bundle which was passed by a free vote in the legislature. For the purposes of this analysis, let us assume that the bundle of programs, which if placed before the electorate and compared with any other bundle would enjoy majority support, is "the wishes of the electorate". Assume for simplicity that there exists only one such most preferred bundle.[10] Suggestions of which bundle reflects the wishes of voters must of course be speculative. The Council is of the opinion that the preferred bundle would not include such extensive regulation of the economy as exists presently. All too often regulations and quasi-judicial agencies have been used to protect special interests which do not command widespread support. It also seems likely that there would be more government activity to secure greater equality of opportunity and a more equal distribution of income.

One can also ask about the costs of reaching decisions in our present system. The transactions costs of the decision-making system appear to be high and rising. Civil servants, lawyers, interest group leaders, consultants, and lobbyists all command resources – far more resources than might be necessary with a smaller government sector or a less concentrated private sector. In the face of inflation and rapid social and economic change individuals have become more uncertain about their relative and absolute well-being. As a consequence, people appear to have organized into groups, and through these groups have sought to secure certainty about their status by having the government protect their interests. Other individuals, again acting in groups, perceiving their relative positions to have been eroded by government actions have sought to have government restore their position. The result is more intensive intergroup conflict that is unlikely to be easily resolved in the short run.

One can also ask whether the process leads to an efficient allocation of resources – all inputs assigned to their most productive use, all commodities assigned among people such that no one can be made better off without

making others worse off, the bundle of products produced by industry matching the relative values placed on them by consumers.

The decision-making process does seem to produce certain outcomes which are not efficient. Programs seem to require more supervisory officials than are necessary, although this proposition is almost impossible to prove because the output of most public programs is so difficult to measure. Many programs, particularly those designed to help low income families, seem to use inefficient methods of assisting beneficiaries. Through redesign, beneficiaries perhaps could be made as well off and fewer resources used. As was discussed earlier in the paper, large income transfer programs have been instituted with apparently little change in the distribution of income.[11] A frequently suggested reform of social security programs is to make sure that only those "in need" receive transfers. These proposals have two main disadvantages: they would require a means test which many people find objectionable, and any program which has both an adequate guarantee for those with no income and a rate of decline in benefits which does not discourage work will imply that transfers will flow to those not "in need". The decision-making system, and the impact of interest groups working within it, seems to have blunted the traditional tools of stabilization. The pressures from various interest groups on overall demand for income appear to have been validated by increases in the money supply.

The system also seems to have made so many changes in policy recently that the level of uncertainty has increased in our society. This phenomenon has recently been receiving belated but necessary attention. Saving or investing to yield future returns requires an environment in which forward planning is possible. If a business is contemplating a new investment the decision will be based on the expected demand for the product, the expected future costs of production and, just as important, prospective future tax, subsidy, regulatory and other government policies. If there is increased uncertainty the expected rate of return required to proceed necessarily rises. Projects that previously would have looked attractive are ruled out because the prospective return is too low with increased uncertainty.

When the policies of governments are constantly changing, investment and saving are adversely affected. Whatever the merits of the wage and price control system, for example, its unfortunate legacy may be a dramatic increase in uncertainty. If controls were used once they can be used again.

Rising uncertainty has effects beyond discouraging saving and investment. Unanticipated policy changes have been a recurrent scenario; unilateral freezes on capital spending in education, seemingly arbitrary hospital closings, and on-again, off-again housing programs have all contributed to the perceived endless increase in the level of uncertainty. University administrations, hospital boards and municipalities find it increasingly difficult to make decisions that would have future ramifications.

Many of the changes in the policies of governments were apparently intended to pursue objectives that command wide support. No one would argue that government policies should not reflect changes in the demands of the citizenry. But it is essential to keep in mind that in our mixed economy, in which many of our common goals are achieved by setting up rules and incentives that influence the decisions of the private sector, frequent and unanticipated rule changes can have perverse effects.

Is there an alternative process with fewer drawbacks? Certain of the more radical commentators have offered suggestions such as requiring a two-thirds majority for the passage of all bills or placing a constitutional limit on the relative size of the public sector, or legislating a breakup of all powerful interest groups (be they unions, corporations or professionals). The disadvantages of these alternatives seem to outweigh their advantages, at least in the minds of most people. The Council agrees that such radical changes are not desirable.

The development of recommendations for change is difficult, however, particularly in light of the model of the political process developed here. This chapter has suggested that our political institutions play a large part in translating 'what we want' into 'what we get'. Exhortations to change the outcome of our political process are often found in political speeches. While the Council recognizes the role of persuasion and supports attempts to increase public awareness of the extent and impact of government activities – indeed much fundamental change results from this approach – it takes the position that an effective stance would be to change the incentive systems under which collective decisions are made. When it pays to spend, spending will be greater than it needs to be. Somehow or other we must change the structure of the system so that it pays not to spend. And changes must be in the self-interest of those who hold the power to change.

The Council is of the opinion that more openness with respect to government activities would reduce the power of special interest groups to secure benefits for themselves and provide an incentive to politicians and civil servants to achieve greater efficiency in the delivery of services. Proposals to strengthen the Committees of the Legislature as one method of achieving this openness deserve serious consideration. The needed changes extend beyond such often cited reforms as televising the proceedings of the legislature or the establishment of codes of behaviour regarding conflict of interest. Changes might include greater reporting of the extent of government activities particularly in the regulatory field; greater investigation of the costs (and benefits) to taxpayers of tax concessions and regulation; and disclosure of the background data used in reaching a government decision. While such reforms can be expected to evoke resistance from those who now gain from the status quo, the apparent growth in voter sentiment in favour of more disclosure makes such reforms more feasible.

In addition to reforms to expand disclosure and reporting, consideration might also be given to more effective methods for substantially increasing the interchange of employment among senior personnel working in the public and private sectors of the economy.

The Council is of the opinion that considerable improvement in efficiency could be realized by increasing information on departmental performance available to the public. This might come about from a strengthened central agency, increased party research staffs, or from independent research agencies. Although the efficiency and effectiveness of government programs are difficult to measure, some estimates could be provided to the public and elected representatives. Evaluations might prove embarrassing to the majority party but this is balanced in part by the possibility of laudatory comments and in part by the recognition that increased efficiency can mean more funds to spend on public programs without the need to raise taxes. These reforms would also help to restrain the power and influence of civil servants.

The Council is of the opinion that the government-engendered conditions which sustain the power and/or influence of interest groups, should be examined and perhaps some of them should be eliminated. The self-regulatory powers of professional groups might be further constrained although they presumably cannot be eliminated. This change appears to be clearly in the interest of the governing party which has the power to effect change.

Although these suggestions are familiar, they are, in the Council's opinion, the basic kinds of reforms required. Sometimes the obvious needs to be restated.

4
Applying the Approach: Four Examples

The previous chapters have outlined a general approach to the analysis of government policy decisions. The approach emphasizes the role played by the decision-making process in determining what government decides to undertake. All participants in this process are considered to be motivated by the same force: self-interest. The interaction of all participants in the decision-making process through lobbying, through the provision of advice, through changing public opinion, through logrolling, and so on determines government policy.

Overall superiority of the approach presented in this paper is not claimed – the Council sponsors research that utilizes other approaches too. The Council is of the opinion, however, that analysis of the decision-making process can contribute significantly to our understanding of existing government programs and provides a sounder basis for the evaluation of future government initiatives.

To illustrate this approach four specific policy issues are briefly discussed below. One example was taken from each of four policy areas on which the Council has been focusing its activities: social security, urban affairs, health and education. Together these examples illustrate a number of facets of the approach suggested in this paper. The discussions of the subdivision approval process and of the financing of higher education illustrate in some detail the decision-making process which society has adopted – obviously many of our decisions are made using mechanisms far more complex than a vote in the legislature – and explore how the adopted decision mech-

anism influences the outcome. The discussions of minimum wage legislation and of hospital reimbursement explore what forces in the decision system seem to prevent the adoption of a desired policy, in the sense of being economically efficient. In each example, the major groups involved are identified. How they stand to gain and lose by a specific decision is discussed. Suggestions about how these groups interact to determine the outcome are offered.

The Use of Minimum Wage Legislation

For many years the Government of Ontario has intervened in labour markets through minimum wage legislation.[12] The first minimum wage legislation, passed in 1920, established rates of pay for female workers. The legislation has since been revised on numerous occasions and has been applied since 1963 to both male and female employees. At various times, the law has sanctioned differences in pay between males and females, between regions of the province, and between various industries. Few such differences exist under the present *Employment Standards Act* except between the construction, tavern, and other industries. At the present time the minimum hourly wage rate in Ontario in the construction industry is $2.90. It is $2.65 in other industries and $2.50 in the tavern industry.

Like many social policies the stated rationale of the program is imprecise. Public statements in support of the legislation by politicians are equally vague. Neither permit a standard to be developed by which the success or failure of the policy could be judged. The minimum wage law seems ostensibly to be directed toward two goals. The first concerns the reduction of poverty: the law attempts to ensure that anyone who is employed full-time will have an income sufficient for a basic minimum standard of living. The second concerns equity: the law attempts to ensure that men and women, young and old, citizen and recent immigrant receive equal pay for equal work.

The intended beneficiaries of this legislation are, of course, those who work for low wages. It is one of a number of alternative possible approaches to assisting this group. Other possibilities include direct cash transfers, provision of subsidies-in-kind (such as free health care, education, housing or food), mobility grants, loans to finance the acquisition of skills and assistance in finding alternative employment.

The minimum wage law, in conjunction with certain manpower training programs, has been a fundamental component of our social policy for the working poor. The recent Federal-Provincial Social Security Review has suggested a direct cash transfer program to assist such persons. In a paper released last year *Issues and Alternatives 1976 – Social Security*, the Ontario

Economic Council suggested that an income supplementation scheme should be used to assist the working poor. As yet such proposals have not been enacted. Indeed in recent years there appears to have been increased emphasis on the minimum wage. Where previously it was increased infrequently, it is now raised frequently and since 1965 has been rising faster than average wages.[13]

The interesting question is why the minimum wage continues to be used to assist the working poor. It is not an effective instrument to use to reduce poverty. The wage rate of an employee is not, and cannot be related to his needs. In Ontario, an unattached individual working full time at the minimum wage rate will have an income above the Family Benefits Allowance for one adult. If however, the individual has a dependent, the income will be below the poverty line (defined as the Family Benefits Allowance for one adult and one child).

The minimum wage law also imposes considerable costs on members of the group it was designed to help. When the minimum wage is raised, presumably above that wage which would prevail in its absence, the price of labour is increased. In response, some employers substitute capital for labour. Some firms go out of business. Some firms refuse overtime or use more part-time staff. In short, the demand for workers falls over time as the minimum wage rises faster than the productivity of certain workers. Although the jobs which continue to exist certainly are higher paying, fewer jobs exist. This is particularly hard on the least skilled for the value of their output to employers is often below the minimum wage and therefore they will not be retained – much less hired. Employers are more likely to hire unskilled workers and train them on the job if, over the training period when the employee's contribution is low, the wage is also low. Many young workers likely remain unemployed because of the minimum wage laws.[14]

The principal beneficiaries of the minimum wage law are those who remain employed at the higher wage rate. Often the beneficiaries are those who, without such legislative protection, would suffer discrimination in the labour market: women and recent immigrants.

The relative size of these two groups – those who are denied employment and those who are able to obtain work at the higher wage – depends on the quantity of labour demanded in those industries which employ workers at the minimum wage and their response to increases in that minimum.

Both of these groups are a small fraction of the voting population and, furthermore, neither is organized or adept at pressing their preferences in the political process. The impact of these groups on legislators is unlikely to be a major factor in the decision process. It seems unrealistic to suppose that minimum wage laws exist, or are used in preference to cash transfers or grants for training, because of the lobbying and voting strength of those who work at the minimum wage (and remain employed).

Groups who may gain or lose indirectly from the minimum wage laws but who are more numerous or better organized than those directly affected are probably important. A frequent supporter of the minimum wage law is organized labour. Most union members are not directly affected by minimum wage law changes. But because wage demands are often based on the claim that traditional relationships should be preserved, a pay hike at the bottom may be used to rationalize a pay hike for those earning substantially more. Furthermore, organized labour benefits from higher minimum wages because such a change raises the price of labour which might be substituted for union workers and therefore helps to secure the jobs of the union members.

The employers of low wage labour suffer as a result of raising wages through increases in the minimum wage. Some firms have their profits reduced. Others have to reduce their level of output. Still others are forced out of business. At the same time employers, who for various reasons find themselves locked into relatively high wage levels, gain from the protection afforded by minimum wage legislation against "low-cost" competitors. Indeed, from the standpoint of both trade unions and many employers, minimum wage laws today, whatever the original intentions, serve a protective function analogous to that served by tariffs and quotas internationally: both protect against "low-cost" competition from relatively inexpensive labour.

The interests of some public servants in pushing Ministers for increases in minimum wage standards are rather subtle but probably significant. Many public servants working in the field of labour-management relations and labour market analysis find traditional economic analysis unsatisfactory. They often believe that raising the minimum wage will either not drive the less productive into unemployment or that if firms cannot survive with a higher minimum wage they deserve to perish. In addition, in recent years at least, the federal government has been the leader in raising minimum wage rates for the few, but crucial, industries under the jurisdiction of its labour legislation. It may be that their provincial counterparts take professional pride in being able to deliver as much, or more, than the federal government. Furthermore, federal and provincial public servants in the labour field sometimes see themselves as representatives of the interests of labour *vis-a-vis* capital (management). This gives them an added inducement to press for labour's interests, as they perceive them.

Where does this leave politicians – those who must ultimately resolve all of these conflicts? Heretofore, although the situation is gradually changing, politicians appear to have perceived that raising minimum wage rates was the prudent course. Those cast into unemployment were inarticulate. Estimates of their numbers and the number of businesses adversely affected were indefinite.

Raising the minimum wage, makes Ministers appear to be benevolent to those clearly at the bottom of each of the occupational ladders without having to spend more of the government's cash (at least directly). The true social costs are well hidden and remain unclear. Higher minimum wages also make it possible for Ministers to claim that they are helping the "working poor" without grasping the extremely thorny issue of direct transfer payments to this group.

The Subdivision Approval Process

In perhaps no area of government have we adopted such an elaborate and complicated system for reaching decisions as in the area of subdivision approval.[15] A minimum of two, frequently three and in some cases four levels of government are involved (local, regional, provincial and federal), each having a significant role in granting the approval. Appointed Planning Boards are an additional vehicle for incorporating the views of planning professionals and citizens. Many of the decisions made in the process of approving a subdivision are subject to review and approval by a quasi-judicial body, the Ontario Municipal Board (OMB). The decisions of the OMB may be appealed through the courts or to the provincial Cabinet. One can ask, both as an analyst and as someone seeking to improve the process, how the decision-making system influences the outcome (for example in terms of what sorts of projects are approved) and how a different decision system might result in a different outcome.

Complexity does not provide sufficient grounds for arguing that a system is ineffective or in need of reform. Indeed there are many reasons for believing that the decision process will of necessity be complicated. Numerous groups have considerable direct and indirect interests at stake in the approval of a subdivision, and in almost every case the actions of one can impose considerable external costs on others. Wherever externalities are involved, a bureaucracy is often required to resolve the conflicts. Consider for example the complex legal system we use to resolve civil suits involving even two parties. The externalities involved in housing matters, whether it be the value of a house or the character of a neighbourhood, seem to be particularly important to the people of Ontario. The public sector has always played a large role in regulating the development of our communities and in resolving potential external costs due to conflicting land uses.

At the most aggregated level a rather simple summary of the decision process may be presented: on the initiative of a private developer a proposal for a subdivision is placed before the provincial Legislature; if it receives the support of the majority of the Legislature, the private developer may pro-

ceed to build the subdivision. This simple schema reflects the fundamental point that a subdivision approval is legitimized by the Legislature of the Province. Of course the approval is not actually granted by the Legislature. The Legislature has delegated its authority and established channels through which any approval must pass. To appreciate the truth of the argument that the method of making decisions is a critical determinant of the outcome, one need only speculate on how different things would be if every subdivision approval did require direct approval in the Legislature.

The most obvious, and most critical, delegation of authority by the Province occurs with the creation of local and regional governments. These local authorities, although in many cases directly elected by the citizens within their boundaries, ultimately receive their legitimacy from the Provincial Legislature.

The legislation establishing the process for approving subdivisions is the Ontario *Planning Act*. A wide-ranging statute applying to both urban and rural areas, it sets out the provincial, regional and local powers regarding land use planning, the subdivision of land and the regulation of land use. The procedures have evolved differently in the different parts of Ontario and are distinctly different as between organized municipalities and unorganized areas. The pattern which is followed in most organized areas can, however, be sketched.[16] It should be noted that the process is presently under extensive review and may be changed significantly over the next several years.

The overall planning at the local level is carried out, not by municipalities within their boundaries, but by planning boards in planning areas; the areas may cover one municipality or several. Local councils may apply to the Minister of Housing to have a planning area defined. The Minister may also of his own initiative establish a planning area. The Minister and his staff set out the boundaries of the planning area and specify the powers and procedures to be followed by the planning board. The members of the planning board are then appointed by the councils of the municipalities subject to the approval of the provincial Minister.

The first responsibility of the planning board is to prepare an official plan, which is intended to be the central document guiding all development within the planning area and to which all developments, especially new subdivisions, must conform. Even the local council must act in conformity with the plan when passing bylaws or providing public works. The planning board, after consultation with the public and the relevant provincial and local agencies, presents a plan to council; the council recommends its adoption and forwards it to the Minister of Housing for his approval. Public disagreement with a plan can require it be referred to the Ontario Municipal Board for a ruling.

The development of a plan for a community is a curious interaction of two levels of government and an appointed body. The preparation of the

plan is separated from the council. Many councils have openly disagreed with their planning board or sought to diffuse its influence. On other occasions, councils have endeavoured to shift the responsibility for making controversial decisions to the planning board. Some councils have not bothered to approve an official plan or even have a planning board established, despite open encouragement from the Province to do so. In other cases the planning boards and councils have put forward plans which the Minister rejected.

In most cases a municipality will have a body of zoning bylaws to which a proposed subdivision must conform as well as an official plan. At present, municipalities receive their authority to pass zoning bylaws under the *Planning Act*, although the authority was granted in other ways before the *Act*. The zoning bylaws can regulate in numerous fields including the use of land, minimum size of lot, density of development, cost and type of construction and even external design and character of buildings.

Zoning bylaws are passed by the municipal council, often after extensive consultation with the planning board, and must be approved by the Ontario Municipal Board. The Province has no direct role in the passage of local bylaws although most are referred by the Municipal Board to interested provincial agencies for comment and suggestions.

It is within the context of an adopted official plan and a set of bylaws that most, although by no means all, municipalities consider a proposal for a subdivision. Technically, a subdivision involves the division of land into smaller parcels for sale or long term lease. This can be done in two ways under the *Planning Act*: one method deals with the submission of a plan of subdivision; the other method deals with parcels described by metes and bounds, known as consents. It is the former process which will be considered here.

It is hypothetically possible that an area which a community thought would be subdivided at some future time could be completely covered by the official plan and a set of bylaws reflecting all the Province's and community's interests in any possible subdivision. When a developer proposed to subdivide the land, the only issue would be whether the proposed subdivision conforms to the plan and the bylaws. This hypothetical case never occurs and, although it might be thought to be the ideal, it is probably not even desirable. The Province and the community could never specify all their interests in advance and no developer would likely want to be forced to market a product whose specifications were designed years before.

The rules and procedures just described are only the environment which surround an actual proposal for a subdivision; the approval process is different again. A plan of subdivision must be approved by the Minister of Housing except in areas with regional governments, where, since June 1975, the right to approve plans of subdivision has been delegated to regional governments.

The approval process is long and complex. A draft plan of subdivision is first submitted to the Minister (or the regional council). It is then circulated through appropriate provincial Ministries (including among others, Housing, Transportation and Communications, Health, and Environment); then circulated through appropriate local and regional departments often under the coordination of the planning board. After the draft plan has been approved the final engineering plans are drawn up and again circulated. The municipality then enters into subdivision agreements with the developer. These agreements govern almost all aspects of the proposed subdivision and are the mechanism which ensures compliance with the draft plan. They can deal with the timing of development; the installation of water and sewer services, roads and sidewalks to certain engineering standards; financial requirements involving lot levies and performance bonds; site plans; and housing standards. The negotiation of subdivision agreements remains the most contentious aspect of the approval process.

In some cases a new development will require an amendment to the official plan and in most cases an amendment to a zoning bylaw. Municipalities often deliberately pass zoning bylaws which are inappropriate for the anticipated future use of the land in order that special restrictions and concessions may be obtained from an applicant during the zoning amendment process. A zoning bylaw amendment must be approved by both the local council and the Ontario Municipal Board. If any objections are filed to the bylaw, an arbitration hearing will usually be held by the Ontario Municipal Board.

After the agreements have been signed, and any zoning changes secured, the draft plan is approved by the Minister of Housing or the regional government. Approval secured, the developer may obtain building permits and commence construction – six months later a home may even be sold.

The entire process from submission of draft plan to approval is long, and appears to be getting longer. A recent research project for the Ontario Economic Council found that the average duration of an application for subdivision approved in 1973 was 1.9 years; in 1974 it was 2.1 years; and in the first half of 1975 it was 2.3 years.[17]

The mechanism we have adopted in Ontario for making decisions on proposed subdivisions is but one of a large number of alternative possible mechanisms. It takes little imagination to conceive of how alternative systems would lead to different results in terms of location, timing and character of the developments approved. At one extreme we could leave the process entirely in the private sector permitting any landowner to do what he wished with his land. Most people in Ontario believe that such a system would produce low quality developments which impose considerable external costs on other residents. At the other extreme the process could be entirely

handled in the public sector as in the case of the development of new towns. Most people believe that such a system would be too inflexible and produce higher cost houses less suited to the diversity of consumer tastes. Alternative mixtures of private and public decision making could be envisaged: for example public planning with construction done under tender; private initiative and planning and complete local control of approvals; or private initiative and provincial control. Each would likely have its own results, just as the current system has its own influence on the outcome.

To illustrate further, consider in particular how the present decision system influences the sorts of developments which are approved. At present the system, particularly in large growing communities, seems to favour approval of developments which have large lots and, by implication, high cost homes. Such developments are in the interests of many individuals and groups within the province and against the interests of others.

The local councils are elected bodies assumed, in the model we have developed here, to be primarily interested in securing re-election. The council therefore will wish to approve those developments which produce the maximum net benefits for their voters and, in particular, those developments which do not raise the taxes of existing residents. For the purposes of this analysis the local council and existing residents may be assumed to have coincident interests. The costs of providing municipal services to new residents vary with their number and also with the number of children; the revenues derived from new residents vary with the assessed value of the residences. Councils will tend to seek developments with a high assessed value per resident or per child, certainly as high as the average assessed values of existing residents, so that taxes will not rise. High per capita assessed values cannot be legislated directly, but may be indirectly secured by requiring large lots. The bylaws which secure these conditions are a municipal responsibility and require only the approval of the Ontario Municipal Board. The Board is primarily interested in seeing that due process has been followed and in hearing the complaints of surrounding residents (who usually share the interests of the council or are even more interested in high quality, expensive developments).

Existing homeowners, an influential subgroup of the voting population, have an interest in seeing the housing values of the community rise. This interest is often therefore shared by the local council. Although frequently argued to the contrary, it is unlikely that any community can significantly influence the price of housing by setting such standards and procedures as to restrict the supply of new housing. The supply of housing under the control of one community (or all communities or all developers for that matter) is too small as a fraction of the total supply of housing to permit significant market power. Maintenance of property values is more likely to be achieved by requiring new communities to be well designed and esthetically pleasing

so that they can then bestow positive external benefits on neighbouring areas.

Developers and builders also have an interest in the nature of a development; they are interested in that type of development which will yield them the highest rate of return. Depending on the state of the housing market in any community at any time, the most profitable type of development can vary greatly. In general however, the higher the density of the development, the higher the rate of return that is likely to be realized. Developers and builders are likely to favour smaller lots and reduced set-backs or no restrictions on the type of unit which can be built. Although private developers present the initial draft plan to a municipality, they have little leverage in the negotiation process except through political support and campaign contributions to municipal councillors.

The interests of the civil service at both the provincial and local levels lie in having extensive constraints on any development and an extensive approval process – this creates and ensures a demand for the services of their bureaus. It is not clear however that this necessitates large lots. As regulators who would seek to ensure that no complaints arise about a faulty product, the officials would tend to favour high quality servicing and construction standards. However, as regulators who would seek to insure that no complaints arise about the price of the product they might tend to support the opposite position, particularly on lot sizes. It is unlikely therefore that government officials have strong interests in these issues, other than to ensure that extensive regulations exist.

One group which has an unambiguous interest in smaller lots is the consumers of smaller, lower priced houses, typically young, middle to lower income families. Their influence is not strong within the decision process. They are a small minority of the population, geographically dispersed – most do not even live in the community which is making the decision on the housing subdivision. The costs of organizing a group to represent their interests would be high and the task extremely difficult because of the free rider problem.

The final participant in the system is the provincial Government. Its potential role in the decision process is enormous – it sets up the rules governing the process, approves the appointments to planning boards, staffs and advises the Ontario Municipal Board, and approves plans of subdivision in areas not covered by regional government. As stated at the outset, the entire process is the creation and responsibility of the Province. It is at the provincial level that the majority of consumers of small lots must make their influence felt. It is only through a provincial member that an individual may have an influence in a community in which he or she does not reside. A majority of provincial voters probably support the principle of relaxing standards. Voters seem to support the general principle at the provincial level but

not those specific measures which would curtail local autonomy nor do they support those candidates at the local level who would institute bylaw changes – certainly many of us favour smaller lots but not in our own community. The Province has attempted to convince the municipalities to change their standards through public statements and by publishing reports which show that smaller lots would reduce housing prices while still permitting a pleasant urban environment. (As an aside, it is interesting to note that both the Province and the development industry have published reports showing the feasibility of small-lot subdivisions and that local governments have strenuously disputed their findings). The Province has offered a small program which gave grants to municipalities in return for permitting low cost housing. The Province has not, however, acted to take away from the local level the power to restrict lot sizes.

The local council through its role in passing bylaws and negotiating subdivision agreements, clearly has the greatest influence in constraining the nature of new housing developments. Although having significant potential influence, the role of the Province has largely been to ensure that proper procedures are followed. The principle of local autonomy has been followed. The interests of individuals and groups who vote in local council elections – the existing residents – will be dominant in the decision regarding the nature of subdivisions. Persons who oppose a bylaw may complain before the Ontario Municipal Board but the problems of organizing potential small-house purchasers have made appeals by this group infrequent. It is likely that more small-lot subdivisions would be approved if this authority to constrain development rested solely at the provincial level. There, one member representing the community containing the new subdivision would confront the remaining members, some of whose supporters are potential residents. Clearly the remaining members, seeing that a new subdivision could be located in their riding in the future, might, through logrolling, oppose the subdivision; but there would likely be more small-lot subdivisions approved.

As is always the case in examining any decision process, the fact that it has certain problems is not sufficient grounds for recommending change – the alternatives may have more problems. There may be sufficient advantages from local autonomy to conclude that the restrictions on lot sizes which result are acceptable. Nonetheless, it is evident that the design of the present decision-making process has an important influence upon the outcome of the process.

Hospital Reimbursement

The past decade has witnessed increasing attention to cost containment within the health care sector.[18] Hospital expenditures accounted for approx-

imately 60 percent of personal health expenditures in Ontario in 1973. In addition, growth in this sector, as measured by expenditures, exceeded almost all other sectors of the economy in recent years. This rapid growth has given rise to increased public and political concern. It has led, in Ontario, to the implementation of a number of specific hospital budgetary changes designed to alter the incentives affecting hospital efficiency and to contain, or even reduce, hospital expenditures. Yet the view of the decision-making process presented here suggests that little improvement could have been expected, as indeed was the case.

In analysing the impact of hospital reimbursement policies it is important to consider the decision-making process within the hospital. Often the hospital is analysed as a single entity pursuing a nebulous objective such as "providing high quality health care". All the principal participants in hospital decisions, from the chief administrator to the duty nurse, are assumed to pursue this objective. Such a view is likely to be a poor guide in the development of health policy. Considerable guidance can be obtained, however, if it is assumed in the analysis that the separate participants pursue their self-interests within the incentive structure of the hospital system. This approach seems to better explain the indifferent success of a number of policies implemented by the Ministry of Health.

The board of trustees, hospital administrator and medical staff (in the university hospital setting it is necessary to add a fourth group, the university administrative body itself) are commonly acknowledged as the three (or four) major participants determining the policies of a particular hospital. In Ontario six other non-Ministry of Health bodies exert some influence: the Canadian Council on Hospital Accreditation, the Ontario Hospital Association, the Ontario Medical Association, the College of Physicians and Surgeons of Ontario, the Ontario Nurses' Association and the Canadian Union of Public Employees. While not without some effect, these latter groups are not considered in the following analysis.

In light of the recent and persisting public awareness of, and concern with, escalating hospital expenditures, the Ministry of Health has set as one of its objectives the reduction, or at least the stabilization of hospital expenditures either through increases in efficiency or decreases in utilization or both. The Ministry has delineated (implicitly if not explicitly) a number of other objectives pertaining to hospital facilities. Among them are efficiency and effectiveness of operation, equity (with respect to the treatment of hospital workers, hospitals and patients) and cost containment.[19]

What then are the roles and interests of the various actors in the hospital decision process, and what might one expect their reactions to be to various Ministry policies?

The board of trustees is largely responsible, in principle, for enforcing Ministry policy and for representing the interests and preferences of the

community. Its functions include the initiation of new programs, appointment of an administrator and determination of the number and type of medical staff affiliations (often in conjunction with a medical advisory committee). The last function, while apparently implying effective control over the mix of care provided, entails limited scope in practice because of the ever increasing professionalization of administrators and the board's dependence on the medical advisory committee for professional advice. To the extent that sitting as a member of the board brings with it a certain degree of prestige which is directly related to the hospital's reputation, the trustees' self-interest lies in maximizing the number of patients treated, or the value of the capital facilities, or the number of well-respected medical staff affiliated with the hospital. In that regard, their objectives will not be unlike those of the administrator whose reputation, and perhaps career, is closely related to the hospital's reputation.

The hospital administrator basically controls the day-to-day functioning of the hospital and is responsible to the board. The administrator's duties include the employment and supervision of all non-medical staff personnel including house staff (although the latter influence is often minimal), responsibility for laundry, housekeeping and other 'hotel-type' hospital services and provision of advice to the trustees about the allocation of the available budget – to the extent that the Ministry permits flexibility. The administrator does not have any direct control over the medical staff. The interests of the administrator are also connected with the prestige of the hospital. Conceivably the pursuit of greater prestige may manifest itself in preferences such as 'bigger is better' or two open-heart surgery units or two renal dialysis units are twice as prestigious as one. On a somewhat less cynical level the administrator's reputation is likely related to the size of the hospital (in terms of patient throughput, rated beds, or scope of facilities), to the prestige of his in-house and medical affiliated staff, and to his hospital's past performance in living within approved budgets without sacrificing quality of care.

The medical staff members are also responsible to the board of trustees, although they retain considerable autonomy through the pertinent activity regulations. They submit recommendations to the board on various matters relevant to the practice of medicine within the physical confines of the hospital. Rarely are such recommendations rejected by the trustees. The admission and duration of stay of all patients is left almost exclusively to the discretion of the medical staff. Assuming that the average physician wishes to maximize net income, subject to a sufficient level of leisure and within the limits enforced by the ethical requirements of the profession, it is clear that the hospital plays a role in generating that income. Hospital facilities provide a relatively inexpensive means (particularly because the time and overhead costs of physicians are minimized by gathering numerous ill pa-

tients in one locale) of practicing medicine. Physicians who are remunerated by fee-for-service have a clear self-interest in encouraging hospital utilization rather than the obvious alternative – house calls for those who are too ill to visit their offices.

Such behavioural hypotheses are not new. They have been discussed *ad nauseum*. However, they are crucial in this particular context because they may serve to elucidate the weaknesses in past Ministry policies.

Two further observations are germane at this point. First, we must not conclude that a fundamental managerial-medical conflict exists. To be sure, some incongruity in objectives may be evident. Counteracting that, however, is the fact that both administrator and medical staff ultimately answer to the board. The medical staff are partially dependent on the hospital for income, so they are anxious that their hospital privileges not be withdrawn by the trustees. The administrator and the trustees are dependent on the quality and morale of the medical staff. Should a rift develop between the administrator and the medical staff the implications are obvious: the administrator may be thought incompetent and his career will probably suffer.

In general, it appears that the medical staff are the dominant force within the hospital.

Equipped with these behavioural insights, and with an elaboration of the self-interest concept in the context of hospital decision-making, consider now a number of changes in hospital financing arrangements: their ostensible objectives, the apparent results, and what might have been expected according to a self-interest theory of behaviour.

The Ontario Ministry of Health introduced a number of hospital budgetary changes during the period 1968-1974. Commencing in 1969, all public general hospitals (except new ones) were shifted from line-by-line budgeting (or cost reimbursement) to global budgeting. This involved a shift from reimbursement of specific 'cost centres' within the hospital for expenditures actually incurred, to a process whereby a budget was submitted in advance and, subsequent to its approval by the Ministry, the allocation of resources within the hospital was at the prerogative of the administrator and board. Concurrent with this shift to global budgeting in 1969 was the introduction of negative incentive reimbursement, so named because, except for permissible cases, hospitals were responsible for meeting any overruns which exceeded the approved budget. From 1970-1973, a variety of positive incentive reimbursements were introduced.

The shift from line to global budgeting in isolation, devoid of the adoption of concomitant negative incentives, was unlikely to markedly affect any aspect of hospital performance because it did not require any particular response on the part of boards, administrators or medical staff. If strict control of "cost centres" under line budgeting had been evident, the shift to global budgeting could have yielded a different mix of care but little else.

The available evidence indicates that rigid control of "cost centres" was absent in Ontario so that it is doubtful that much was achieved.

The Ministry apparently felt that global budgeting, by separating the growth of expenditures into two components – wages and prices, and the level of activity – and by ensuring that all hospitals were equitably treated with regard to the former, would help to contain that growth. Yet such a scheme ignores the factors involved in hospital utilization, factors largely controlled by the medical staff. To the extent that the shift in budgeting methodology did not change the incentives faced by practitioners it is hardly surprising that the new scheme has apparently had little impact.

When coupled with negative incentive reimbursement (whereby hospitals are responsible for overruns) that conclusion requires modification, but only to the extent that the threat of overruns affected the practices and procedures of physicians within the hospital. The administrator could exercise the option of cutting corners in non-in-patient related areas, or in areas which did not affect physician practices because it was, and still is, in his interest to contain costs while maintaining harmony with the medical staff. The evidence appears to indicate that negative incentive reimbursement achieved at least the cost containment goal of the Ministry by tending to hold hospitals to their budgets. Its influence on efficiency appears to have been negligible.[20]

The positive incentive reimbursement scheme was even less successful. This was due in large part to the nature and size of the potential savings which could accrue to the hospitals. In particular, hospitals which spent less than their approved budgets were given the choice between a continuous, or a one-time award. The former was intended for cases in which the hospital in question anticipated a continuation of a given year's underrun. The hospital could then claim 90 percent of the difference between actual and approved expenditures, in which case its budget was immediately revised downward to the actual expenditure level, with little expectation of subsequent activity adjustment or revisions for inflation. Alternatively, the hospital could accept lesser and declining awards over a number of years, accompanied by a less rapid decrease in future approved budget levels.

The one-time awards were intended for cases when the underrun was expected to last only one year. The awards amounted to 10 percent of the shortfall, with no concurrent revision to the approved expenditure level. The hospital could opt for one-time awards in lieu of a continuous award. Despite the apparent attractiveness of the continuous awards, the awards actually accepted were almost exclusively of the one-time nature, regardless of the nature of the underrun. This was undoubtedly due, in part, to the failure of the Ministry to uphold the conditions of the originally intended package, which would have allowed budget revisions for activity adjustments and

inflation adjustments subsequent to the acceptance of a continuous award.

Clearly, positive incentive reimbursement was intended as an efficiency improving/cost reduction measure by the Ministry. To the extent that it was a failure, blame must fall with the design and magnitudes of the positive *vis-a-vis* the negative incentives. Administrators and boards have, as one objective, the covering of costs under a 100 percent penalty, as embodied in the negative incentives. But the Ministry appears to have undermined the positive incentives by reneging on its agreement to use the previous year's approved expenditures as the base and proceeded, instead, to apply the previous year's actual expenditure levels. Those hospitals which managed to stay within their previous year's budgets, or even saved on the approved amount, were penalized in subsequent years.

The positive incentive scheme was further weakened by the size of the one-time awards (ten percent), which could hardly be thought of as an adequate incentive. In addition, the scope for using such a limited reward was curtailed by the Ministry's veto power over the implementation of new programs by a hospital.

It seems evident that the interests of boards and administrators in achieving cost savings have been little increased, although the pressure to avoid cost overruns has certainly been greater. Finally, it should be emphasized that the positive and negative incentive programs, even if implemented in a more desirable manner, were both intended to affect the decisions of administrators and board members. But it is the decisions of the physician that are crucial and the policy changes do not appear to have had any impact on them.

It appears that so long as hospitals are dependent upon the Ministry for a major share of their operating expenses and so long as the Ministry fails to provide a reimbursement scheme which is cognizant of the varied, yet closely related, objectives of hospital decision-makers, cost containment may be little more than a dream. Insofar as hospital expenditures, when unchecked, tend to grow more rapidly than expenditures for alternative goods and services and utilize limited resources, the implications for other public services, in the absence of further tax increases or some form of patient deterrent fees, are obvious.

Perhaps the answer lies in making physicians more aware of, and partially accountable for, the expenses entailed in the utilization of in-patient hospital facilities. At the same time, Ministry officials must ensure that there is no incentive to medical staff to cut corners where doing so would imperil a patient's health.

A neutral incentive scheme is required under which the physicians themselves would not attain relatively higher net returns from the hospital based treatment of a particular illness if an alternative exists.

Financing Higher Education

Universities and colleges may be thought of as licensing bodies. The degrees or certificates they award are a kind of approbation: an acknowledgement of the possession of a minimum standard of education as well as perhaps a certain amount of patience and persistence. The value of the certificate is, of course, not independent of the reputations of those who place it there. The individuals who are accredited may be of equal worth, in some sense, but it is the reputation of the faculty members that makes the degree of one university more credible than that of another.

It is important to recognize that it is the state, in effect, that grants higher educational institutions licensing powers and thereby confers a certain legitimacy upon the pieces of paper they bestow on their students. One of the questions that governments must face is the allocation of this licensing power among a variety of existing and prospective educational institutions.

Another question is the extent to which students should have to pay their own way.[21] This raises all kinds of questions about equality of opportunity – a widely accepted goal in our society. At one end of the spectrum is the pay-as-you-go option that, given the costs involved in most post-secondary education, would effectively exclude children from lower and middle income families. At the other end of the range of possibilities would be free tuition and fully subsidized living costs.

Making post-secondary education a "free good" in this way would give benefits, that are not required, to the children of wealthier families. But it would still not help the children of lower income families who must earn an income early in life to help support themselves, their siblings and often, indeed, their parents.

Between these two extremes there are a multitude of possibilities. To what extent should the total cost be borne by the taxpayer relative to the student? What proportion of the taxpayer's support should be in the form of grants? What proportion in the form of subsidized loans? If the loan proportion were high, should the unsuccessful graduates or graduates with low incomes be forgiven?

The conflicts that bedevil higher education involve several groups. There are the students (and their parents) who want low fees, loans on generous terms, small classes, exciting lectures and certification on completion. There are university and college teachers who want light teaching loads, freedom to pursue their own research interests, freedom to speak up on controversial topics, security of tenure and generous financial compensation. There are university and college administrators who seek to resolve the conflicts between the two bargaining groups, the conflicts among competing institutions and the conflicts among the instutions that each want to maintain their "independence" while obtaining more funds. There are governments that

provide most of the money. Governments, of course, want to contain their outlays of funds, avoid criticism from teachers and *appear* to be facilitating educational opportunities for everyone – particularly the bright children of lower income families. At the same time, it cannot be ignored that ensuring the educational progress of the children of the affluent and the influential is not without its political payoff.

These then are the principal actors and a sketch – almost a parody – of their motives. How is the decision-making process organized in order to resolve, as distinct from "solve", the never-ending conflicts among them?

There are faculty associations; there are student councils; there is the Council of Ontario Universities; there is the Ontario Ministry of Colleges and Universities; there is the Ontario Council on University Affairs (OCUA); there is the Secretariat for Social Development; there is the Secretary of State in Ottawa responsible for the federal contributions to student aid. There is also the Association of Universities and Colleges of Canada (AUCC). One could go on.

It is impossible in this short compass to describe, much less analyse, the everchanging and perpetual relationships among all of these groups or the rules (incentives) that shape their behaviour – the behaviour of the members of groups *vis-a-vis* one another and the behaviour of groups *vis-a-vis* one another. Perhaps our purpose can best be served by considering the role of OCUA.

This group was established to act as a buffer between educational institutions which want both more cash and more autonomy, on the one hand, and the government of Ontario which wants economy (money is painful to raise!), an effective educational system and access for the children of the disadvantaged, on the other.

This way of putting the issue undoubtedly overstates the case. It is true, nevertheless, that there are conflicts between the two groups on the several fronts just cited. OCUA was established to act as a kind of independent buffer that would put the arguments of each to the other with impartiality. The members of OCUA purport to represent "the community" as distinct from the direct interests of universities and colleges on the one hand and the direct interests of the government (and senior government officials) on the other.

There is a paradox that perhaps should be brought to the attention of our readers. The ideological assumption of our parliamentary system is that the elected representatives to the legislature represent "the community interest". For obscure reasons – reasons we have not even tried to explore – legislatures now are not perceived to be truly representative of the communities that elected them so that independent bodies, such as OCUA have to be created.

OCUA appears to have been successful in prodding the Government of

Ontario into providing more cash in aggregate for post-secondary education than otherwise have been forthcoming. At the same time OCUA has taken responsibility for recommending how "the pot" should be allocated among the institutions – an onerous task that both the politician and civil servant are only too pleased to delegate to an independent body that must take the inevitable flak when institutions fight for higher relative positions.

What immediately impresses the observer is the extreme importance of publicity. If OCUA were not independent and did not publish its requests for additional funds (in aggregate) for post-secondary education, the Government could more easily reject the demands of the universities and colleges as just another instance of special pleading by an interest group. The independent, community-representational character of OCUA makes it much more difficult for the government to ignore the published recommendations.

As in the other examples the decision-making process almost certainly has had an impact on the policy outcome, for good or for ill.

Notes

[1] An excellent discussion of the problems of measuring the relative size of the government sector can be found in Bird, R., *The Growth of Government Spending in Canada*, Canadian Tax Foundation, 1970.

[2] For a discussion of measuring the output of the health care sector see Culyer, A. J., *Health Status Measures and Health Care Planning*, a report submitted to the Ontario Economic Council, (mimeo) 1976.

[3] For a discussion of the problems of defining and measuring the impact of government on income distribution see Reuber, G. L., "The Impact of Government Policies on the Distribution of Income in Canada: A Review", University of Western Ontario, (mimeo) 1976.

[4] For a discussion of the measurement of money income distribution, see *Issues and Alternatives 1976 – Social Security*, Ontario Economic Council. For recent data on income distribution, see *Income Distributions by Size in Canada, Preliminary Estimates*, (Stats. Can., 13-206, annual).

[5] The recently published studies include Maslove, A. M., *The Pattern of Taxation in Canada*, Economic Council of Canada, 1972; Dodge, D. A., "Impact of Tax Transfer and Expenditure Policies of Government on the Distribution of Personal Income in Canada", *Review of Income and Wealth*, March, 1975; Gillespie, W. I., *The Redistribution of Income in Canada, An Analysis of the Incidence of Taxes and Public Expenditures in the Canadian Economy*, research monograph (mimeo), March, 1975.

[6] Gillespie, W. I., "On the Redistribution of Income in Canada", *Canadian Tax Journal*, July-August 1976.

[7] The Ontario Economic Council has sponsored several research projects in this area. For a survey of the major works in the literature see Hartle, D. G., *A Theory of the Expenditure Budgetary Process*, published for the Ontario Economic Council by the University of Toronto Press, Toronto, 1976.

[8] In order that this theorem hold, it is necessary that voters have a single most preferred option. It is also necessary to ignore the "voting paradox" which argues that the voting rule used here may not produce a stable outcome.

[9] This example is derived from one presented in Tullock, G., *The Vote Motive*, Hobart Paperback No. 9, The Institute for Economic Affairs, London, 1976.

[10] Again it is necessary to ignore the possibility of the "voting paradox" and to assume certain types of voter preferences (see footnote 8).

[11] See the section "Government and a Just Distribution of Income" in Chapter Two of this report. For examples of these kinds of inefficiencies see *Issues and Alternatives 1976 – Social Security*, Ontario Economic Council.

[12] For a broad overview of the issues involved in minimum wages and social security policy see *Issues and Alternatives 1976 – Social Security*, Ontario Economic Council. For a more detailed discussion of minimum wage legislation see: Silberman, U. E. and Durden, G. C., "Determining Legislative Preferences on the Minimum Wage: An Economic Approach" *Journal of Political Economy*, Vol. 84, April 1976; Stigler, G. J., "The Economics of the Minimum Wage Legislation", *American Economic Review*, Vol. 36, June 1946; Whittingham, F., *Minimum Wages in Ontario: Analysis and Measurement Problems*, Kingston, Queen's University, Industrial Relations Centre, 1970.

[13] For a discussion of recent changes in the minimum wage law see *IR Research Reports*, Vol. 1, No. 2, November 1976.

[14] For a discussion of measuring the effects of minimum wage laws on employment see: Whittingham, op cit.; and Lester, R. A., "Employment Effects of Minimum Wages" *Industrial and Labor Relations Review*, January 1960; Kaun, D. E. "Minimum Wages, Factor Substitution, and the Marginal Producer", *Quarterly Journal of Economics*, August, 1965.

[15] For a broad overview of the issues involved in municipal zoning and housing policy see *Issues and Alternatives 1976 – Housing*, Ontario Economic Council. For a more detailed discussion of municipal zoning legislation see: Mills, E. S. and Oates, W. E., "The Theory of Local Public Services and Finances: Its Relevance to Urban Fiscal and Zoning Behaviour" and White, M. J. "Fiscal Zoning in Fragmented Metropolitan Areas" in *Fiscal Zoning and Land Use Controls*, Mills, E. S. and Oates, W. E. editors, D. C. Heath and Company, Lexington, Massachusetts, 1975, Tiebout, C., "A Pure Theory of Local Expenditures", *Journal of Political Economy*, October 1956; Margolis, J., "On Municipal Land Policy for Fiscal Gains", *National Tax Journal*, September 1956; Sproule-Jones, M., "A Description and Explanation of Citizen Participation in a Canadian Municipality", *Public Choice*, Spring, 1974.

[16]This description is derived mainly from *Subject to Approval: A Review of Municipal Planning in Ontario*, Ontario Economic Council, 1973.

[17]See a report prepared for the Ontario Economic Council, Muller, R. A., *The Market for New Housing in the Metropolitan Toronto Area*, (mimeo) 1976.

[18]For a broad overview of the issues involved in hospital reimbursement and health policy see *Issues and Alternatives 1976 – Health*, Ontario Economic Council. For a more detailed discussion of issues in hospital reimbursement see: Ontario Ministry of Health: *Report of the Minister's Committee of Inquiry into Hospital Privileges in Ontario*, January, 1972; Ontario Ministry of Health: *The Effect of Fiscal Constraints on Hospital Employees*, 1974; Newhouse, J. P., "Toward a Theory of Non-Profit Institutions: An Economic Model of a Hospital", *American Economic Review*, 1970.

[19]See a report prepared for the Ontario Economic Council, Milne, R., *Hospital Budgetary System in Ontario*, (mimeo), 1977.

[20]Milne, R., *op. cit.*

[21]For a broad overview of the issues involved in financing higher education and education policy see *Issues and Alternatives 1976 – Education*. For a more detailed discussion of the financing of higher education see: Association of Universities and Colleges of Canada: *Commission on Financing Higher Education in Canada* (Bladen Report), University of Toronto Press, 1965; Council of Ontario Universities: "Brief to the Canadian and Ontario Governments on the Financing of Higher Education in Canada", Ontario 1976; Hartle, Douglas G., "The Financing of Higher Education in the '70's", *Canadian Journal of Higher Education*, Vol. III, No. 2, 1973; Ontario Commission on Post-Secondary Education in Ontario: *The Learning Society*, Report of the Commission (Wright Commission), 1972. Ontario Queen's Printer; Peitchinis, S. G., "Financing Post-Secondary Education in Canada", Published by Ministers of Education in Canada, Toronto, 1972.

Appendix

Table 1

RATIO OF GOVERNMENT EXPENDITURES TO GROSS NATIONAL PRODUCT

Year	Ratio of Government Expenditures[1] to GNP	Ratio of Government Transfers to GNP	Ratio of Government Expenditures on Goods and Services and Capital Formation to GNP	Ratio of Government Expenditures on Goods and Services and Capital Formation to GNP (Constant 1971 Dollars)
1975	.413	.170	.243	.235
1974	.391	.158	.232	.232
1973	.370	.146	.224	.221
1972	.382	.149	.234	.230
1971	.377	.140	.236	.236
1970	.364	.133	.231	.237
1969	.341	.124	.217	.224
1968	.337	.121	.216	.231
1967	.329	.116	.213	.230
1966	.309	.105	.204	.223
1965	.299	.104	.195	.218
1964	.296	.106	.190	.217
1963	.303	.108	.194	.223
1962	.307	.109	.198	.232
1961	.308	.109	.199	.235
1960	.297	.120	.177	.212
1959	.299	.111	.178	.216
1958	.286	.105	.181	.222
1957	.266	.090	.175	.216
1956	.257	.083	.174	.218
1955	.263	.088	.175	.229
1954	.274	.093	.181	.245
1953	.264	.086	.177	.247
1952	.269	.087	.182	.255
1951	.236	.077	.159	.222

Sources: Statistics Canada, National Income and Expenditure Accounts, Vol. 1, March 1965 (Cat. 13-531 Occasional), Tables 2, 6, 7, 17, 49.

1975 Figures from Statistics Canada, CANSIM, September 1976.

[1] Government expenditures include:

i) Expenditures on Goods and Services
ii) Capital Formation
iii) Transfer Payments to Persons, Business and Non-Residents
iv) Interest on the Public Debt.

Table 2

PERCENTAGE DISTRIBUTION OF GOVERNMENT EXPENDITURE ON GOODS AND SERVICES AND CAPITAL FORMATION BY LEVEL OF GOVERNMENT

	Level of Government		
Year	Federal	Provincial	Local
1975	24.2	42.7	33.1
1974	25.5	41.2	33.3
1973	25.3	40.5	34.2
1972	25.1	40.4	34.5
1971	24.9	39.7	35.4
1970	25.5	38.0	36.5
1969	27.4	35.1	37.5
1968	28.0	35.2	36.8
1967	28.5	35.0	36.5
1966	29.5	33.7	36.8
1965	29.5	32.8	37.7
1964	31.0	32.8	36.2
1963	31.9	31.3	36.8
1962	34.8	29.7	35.5
1961	36.6	29.8	33.6
1960	39.1	23.5	37.4
1959	42.0	22.5	35.5
1958	45.2	21.3	33.5
1957	46.4	21.1	32.5
1956	48.6	20.6	30.8
1955	50.7	18.6	30.7
1954	52.6	17.5	29.9
1953	56.5	16.7	26.8
1952	56.2	17.7	26.1
1951	50.2	20.4	29.4
1950	41.3	24.2	34.5

Sources: Same as Table One.

Table 3

PERCENTAGE DISTRIBUTION OF GOVERNMENT TRANSFERS BY LEVEL OF GOVERNMENT

	Level of Government		
Year	Federal	Provincial	Local
1975	66.2	29.4	4.3
1974	65.2	29.9	4.9
1973	63.1	31.9	6.1
1972	62.4	31.2	6.4
1971	58.6	34.0	7.4
1970	60.9	32.0	7.2
1969	60.9	32.4	6.7
1968	62.5	30.6	6.9
1967	64.6	28.5	6.9
1966	67.5	25.4	7.2
1965	68.4	24.4	7.2
1964	71.0	21.9	7.1
1963	72.1	20.9	7.1
1962	72.4	20.5	7.1
1961	73.5	19.5	7.0
1960	67.5	26.6	5.9
1959	69.4	24.8	5.7
1958	72.9	21.7	5.4
1957	71.7	22.6	5.7
1956	71.9	22.8	5.3
1955	72.8	22.2	5.0
1954	73.1	22.0	4.9
1953	74.2	21.3	4.4
1952	75.6	20.3	4.1
1951	67.4	28.5	4.1

Source: Statistics Canada, CANSIM, September 1976.

Table 4

GOVERNMENT EMPLOYMENT AS A PERCENTAGE OF TOTAL CIVILIAN WORK FORCE IN CANADA 1961-1975

Year	Total Civilian Work Force (000's)	Total Government Employment (000's)	Percentage
1975	10,015	1,183	11.8
1974	9,662	1,129	11.7
1973	9,279	1,078	11.6
1972	8,891	1,031	11.6
1971	8,631	986	11.4
1970	8,374	937	11.2
1969	8,162	913	11.2
1968	7,919	853	10.8
1967	7,694	862	11.2
1966	7,420	808	10.9
1965	7,141	756	10.6
1964	6,933	688	9.9
1963	6,748	670	9.9
1962	6,615	649	9.8
1961	6,521	650	10.0

Sources: Statistics Canada, The Labour Force (CAT. 71-001)
Statistics Canada, Federal Government Employment (CAT. 72-004)
Statistics Canada, Provincial Government Employment (CAT. 72-007)
Statistics Canada, Local Government Employment (CAT. 72-009)

Table 5

RATIO OF ONTARIO GOVERNMENT EXPENDITURES ON GOODS AND SERVICES AND CAPITAL FORMATION TO GROSS PROVINCIAL EXPENDITURE

Year	Ratio
1975	.171
1974	.159
1973	.159
1972	.168
1971	.169
1970	.166
1969	.149
1968	.148
1967	.141
1966	.138
1965	.131
1964	.128
1963	.135
1962	.131
1961	.123
1960	.106
1959	.103
1958	.100
1957	.093
1956	.088
1955	.087
1954	.083
1953	.071
1952	.077
1951	.074

Sources: 1970-1975, Ministry of Treasury, Economics and Intergovernmental Affairs, Central Statistics Service.

1951-1969, Ontario Statistical Centre, Ontario Statistical Review, 1973.